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QUALIFIED INDUSTRIAL ZONES IN EGYPT

Opportunities for Export Diversification

July 2015

This publication was produced for review by the United States Agency for International Development. It was prepared by the advisers supporting USAID's Trade Facilitation Project in Egypt. The authors' views expressed in this publication do not necessarily reflect the views of USAID or the United States Government.

QUALIFIED INDUSTRIAL ZONES IN EGYPT

Opportunities for Export Diversification

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Submitted to:

USAID

Submitted by:

Nathan Associates Inc.

Under Contract No.

AID-263-C-11-00003

July 12, 2015

Egypt Trade Facilitation Project

Contract No. AID-263-C-11-00003

Contractor: Nathan Associates Inc.

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ABBREVIATIONS

| | |
|---------|---|
| CBP | Customs and Border Protection |
| CE | Conformité Européene (European Conformity) |
| CIF | Cost, Insurance and Freight |
| FOB | Free On Board |
| FTA | Free Trade Agreement |
| GSP | Generalized System of Preferences |
| HS | Harmonized System (of Customs Codes) |
| MIFT | Ministry of Industry and Foreign Trade |
| MITSMES | Ministry of Industry, Trade, and Small & Medium Enterprises |
| MFN | Most-Favored Nation |
| NAV | Not Ad Valorem |
| NES | Not Elsewhere Specified |
| QIZ | Qualified Industrial Zone |
| RMG | Ready-Made Garments |
| TFP | Trade Facilitation Project |
| UL | Underwriter's Laboratories |
| U.S. | United States |
| USAID | United States Agency for International Development |
| WTO | World Trade Organization |

EXECUTIVE SUMMARY

QIZ PROGRAM

USAID/Egypt asked the Trade Facilitation Project (TFP) to examine the prospects for diversifying exports under Egypt's Qualified Industrial Zone (QIZ) program into four industrial sectors. The QIZ program was established in 2005 between Egypt, Israel, and the United States as an amendment to the U.S.-Israel Free Trade Agreement (FTA). Products manufactured in an Egyptian QIZ can be exported to the United States at a zero tariff rate; provided the product satisfies QIZ protocol requirements for rules of origin and value addition (at least 10.5 percent Israeli in a total 35 percent combined Egyptian input by value).

Since 2005, the QIZ program has become a significant channel for Egyptian exports to the United States, accounting for close to \$1 billion of exports annually. QIZ exports make up about 45 percent of all Egypt's exports to the United States, but only about 2 percent of Egypt's total exports. The product sector that has taken the greatest advantage of the QIZ program has been clothing and textile articles. In 2014, more than \$800 million worth of woven and knitted clothing (were exported from Egypt's QIZs to the United States. Few industries besides RMG manufacturing export under the QIZ program, with non-RMG products making up less than 6 percent of QIZ exports in 2014.

Diversification of QIZ exports could help create more jobs in the export sector and increase foreign exchange earnings, which in turn would contribute to economic development and poverty reduction. Diversification into other sectors should also mitigate risks associated with market shocks and cyclical shifts in the RMG industry. This report looks at the prospects for product diversification in four industrial sectors that might benefit from exporting under the QIZ: footwear, leather accessories, processed foods, and light manufacturing.

ADVANTAGES OF QIZ EXPORTS

The singular advantage of QIZ status for any export firm is that such status qualifies the firm's products (that comply with content requirements) to enter the U.S. marketplace duty free. This is an advantage sought by importers in the United States as well as exporters in Egypt. The gross value of QIZ status to an exporter or importer, therefore, depends on the monetary value of the duty exemption—the duty they would otherwise have to pay if the products were not QIZ certified.

The actual value of QIZ status to an exporter is likely to be less than the full tariff value for several reasons. First, the costs of meeting QIZ requirements—significantly transforming the product within the QIZ, meeting Israeli and Egyptian value-added thresholds, and satisfying rules of origin—as well as the administrative and logistics costs of locating and producing within a QIZ. Second, the QIZ-certified import must still compete against imports from other countries that also have duty-free status. Third, Egypt could be farther from major U.S. markets (e.g. California and U.S. Western coast) than other countries competing in the same product categories so that potentially higher shipping costs or less-frequent route service could reduce the advantage and accrued value of duty-free Egyptian products. It is important therefore to consider the value of tariff exemptions from the viewpoint of the U.S. importer who has to pay (or not pay) the tariff to take ownership of the goods. If we assume a certain good is subject to a tariff rate of 10 percent, for example, and a U.S. buyer can buy that good

from Vietnam for a landed (pre-customs) price in the United States of \$200 per unit, the buyer will be interested in the same product from a QIZ in Egypt only at a landed pre-customs price of less than \$220 per unit.

The United States' posted tariff rates on most imports are low, with many products entering at a zero rate. This fact narrows and reduces the QIZ program's singular advantage. There are about 17,000 product lines in the Harmonized System (HS) Customs Tariff Code at the 8-digit level. Fewer than 4 percent of those product codes carry tariffs higher than 15 percent. Moreover, the historical trend is that U.S. tariff rates decrease over time. The average tariff on all imports entering the United States is less than 3 percent.¹ So, there is no value to be derived for the QIZ program's tariff-exempt status for any product that is already entering at a zero or near-zero tariff rate. Similarly, for any product subject to most-favored nation (MFN) treatment for which the listed tariff is less than 5 percent or even 10 percent, the QIZ-related tariff advantage is considered insufficiently attractive to justify a business's investment.

The QIZ protocol is an extension to the U.S.-Israel FTA; it offers certain tariff-preference advantages to US importers and Egyptian exporters, but it is only one of 14 FTAs that the United States has signed with 20 countries.

Many of the more sophisticated U.S. firms importing products from overseas employ experts who study U.S. customs agreements and compare all the advantages and disadvantages of importing from a variety of sources. These experts keep track of U.S. trade agreements—tariff advantages and requirements—and consider the overall landed cost of the product in the United States, including any tariff advantage. In addition, these supply chain managers or sourcing analysts take into account other important factors, including reliability of supply, political risk, and instability. So even Egyptian products with certified QIZ status can face stiff competition for buyers in the United States from producers in other countries with FTAs or other preferential tariff treatment agreements.

QIZ EXPORTS TO DATE

The first QIZs in Egypt began operating in 2005. Exports rose quickly, to just over \$1 billion per year in 2011, but dropped to \$920 million (8.8 percent) by 2014.

The first exporters to make extensive use of the QIZ program were in the RMG industry, and clothing has been the dominant export ever since. In 2011, more than 95 percent of Egypt's QIZ exports consisted of RMG (woven and knitted clothing). By 2014, that percentage had decreased to 88 percent.

A small percentage of Egypt's QIZ exports is made up of food—processed, or otherwise prepared. Food exports from QIZ increased 4 percent by value from 2011 to 2014, but the share of food to total exports increased only slightly, from 1.5 percent to 1.7 percent.

Approximately 250 Egyptian companies export annually under the QIZ Protocol out of the more than 585 firms that have been approved to participate in the program.

¹ World Bank. World Development Indicators: Tariff Barriers. 2013. <http://wdi.worldbank.org/table/6.6>

For many private sector firms in RMG and other sectors the main factors governing their decisions to operate under and utilize QIZ status are business competitiveness issues (cost and market linkages) or the difficulties in meeting specific QIZ requirements for Egyptian and Israeli value-added content and the cost to import the Israeli content.

For some Egyptian firms furthermore, personal antipathy or public stigma may be attached to partnering with an Israeli firm, although the QIZ Unit at the Ministry of Industry, Trade, and Small and Medium Enterprises (MITSMEs) provides trade facilitation services to link Israeli suppliers to Egyptian producers at arm's length.

CONCLUSIONS

Initial research suggests that there are few industries other than RMG where the three factors of U.S. market demand, the QIZ program's tariff exemption benefits, and the global competitiveness of Egyptian manufacturers all combine to favor development of export industries in the QIZ framework.

Engineered or light manufactured products are unlikely to benefit from QIZ status, because U.S. tariffs on these products are already very low. Egypt has firms that are globally competitive exporters of engineered products, but the data indicates that these products are being sold in markets in the European Union and elsewhere—not in the United States.

Leather footwear exports are also unlikely to benefit despite high tariffs on a limited set of items. Most footwear enters the United States at duties of less than 10 percent, and any footwear exporter from Egypt would face strong competition from the cluster of mega scale producers in China and East Asia. The Chinese cost advantage over Egyptian producers is likely greater than 10 percent. Egypt could try for a niche export of certain types of high-valued and high-tariff protected shoes, but this would take investment, time, and resources on a significant scale. Ideally, Egyptian producers could identify and integrate into a U.S.-oriented footwear supply chain, where U.S. firms would support product development in Egypt while taking advantage of the QIZ program. Egyptian manufacturers today face problems of scale, quality, cost and environmental pollution (see section below for leather accessories). Investment would need to be made in new technology to upgrade Egyptian shoe quality while lowering costs to successfully integrate its products successfully into its supply chain. The costs to be incurred would be significant in relation to the prospective tariff advantage.

In general, **leather accessories** are unlikely to benefit from the QIZ program despite tariffs as high as 20 percent, because of low-quality inputs and products, and environmental and health concerns about those products. Cowhides are of low quality and collected semiannually, skilled and unskilled labor is hard to find, and firms do not use modern production technology. In addition, tanneries produce cured hides with chemical and dye residue that do not meet U.S. consumer and environmental protection standards. Some leather accessories are anecdotally reported to be included in RMG products exported to the United States, such as in a belt added to a dress, but the belt would be subsumed in the tariff code applicable to the dress, and these additions cannot be disaggregated using HS codes. What is more, much of the leather accessories industry is oriented to the European market, with Egyptian shoe, purse, and luggage producers engaged with Italian buyers and trade shows.

Processed foods present the most likely possibilities for extension of the QIZ program. Tariffs on some products are high enough to encourage a closer look at the potential

advantages. Although food does not have to be cultivated within a QIZ, the producer must demonstrate that the food was substantially transformed within the QIZ to receive the exemption from U.S. Customs. Processed foods have already increased slightly as a share of total QIZ exports. From an economic development perspective, processed foods offer the advantages of a better multiplier impact on the Egyptian economy than would an industry such as leather footwear, which would require the large-scale importation of inputs. The backward linkages would also probably have a stronger impact on poverty reduction.

Expansion of the QIZ program to Upper Egypt, reducing the value-added or substantial transformation requirements could increase export diversity as firms export more agricultural and consumer products. However, if Egyptian firms have not yet managed to generate significant new QIZ products in the relatively advanced business and manufacturing environs of existing QIZ zones, it would seem unlikely that they could do so quickly in the less developed area of Upper Egypt.

I. BACKGROUND AND APPROACH

The QIZ program in Egypt is a U.S. preference program based on an amendment to the US-Israel Free Trade Agreement (FTA) that grants duty-free treatment to qualifying exports from Egypt entering the commerce of the United States, provided they meet certain requirements, including a minimum percentage of inputs from Israel. In Egypt, the program is administered and overseen by the QIZ Unit in the Ministry of Industry, Trade and SMEs². In 2014, \$920 million of Egyptian exports to the United States qualified for QIZ status and treatment.³

USAID ASSISTANCE FOR QIZ

After the signing of the United States-Israeli-Egyptian QIZ protocol in 2005, USAID supported the then–Ministry of Trade and the QIZ Unit through the Assistance for Trade Reform (ATR) project. Several USAID projects since then have continued to provide assistance and study ways of building on the early success of the QIZ program.

The Egypt Trade Facilitation Project (TFP) (AID-263-C-11-0003), implemented by Nathan Associates Inc., is a USAID technical assistance project that focuses on reducing barriers to trade and creating more efficient internal and external trading systems. TFP began June 1, 2011 and is contracted to end on July 31, 2015. In 2012, USAID asked TFP to consider what assistance the QIZ Unit needed to improve efficiency and maximize benefits from the QIZ Protocol. TFP conducted a rapid assessment of the QIZ Unit’s operations and needs in December 2012.⁴

THIS ASSIGNMENT

In May 2015, USAID assigned TFP to update the sections of the 2012 QIZ report related to prospects for diversifying exports from the QIZ in four product areas: footwear, leather accessories, processed foods, and light manufacturing products. A copy of the scope of work for the assignment is in Appendix C. The team carried out most of the research for this activity in May and June, 2015.

²The QIZ Unit’s main responsibilities are: (1) registration of QIZ companies and Israeli partners; (2) certification that products comply with protocol requirements; and (3) quarterly reports on quantities exported prepared for the three partners to the Agreement, USA, Egypt and Israel.

³ Figures from www.qizegypt.gov.eg. Appendix A gives more information about the QIZ program and QIZ unit.

⁴ The TFP report recommended improving IT equipment and staff training that the TFP project went on to support with project funds. The report also raised concerns about the lack of sustainable funding for QIZ operations.

METHODOLOGY

The main objective of this report is to answer the question: “Can certification as a QIZ exporter help an Egyptian firm successfully export selected products to the United States from one of the following four sectors: footwear, leather accessories, processed foods, and light manufactured products?” The simple question is, “Which of these products has a sufficiently high tariff that QIZ status (which QIZ certified exporters will not have to pay) gives a sufficient price or margin advantage over non-QIZ suppliers?” The more complex question is, “Will QIZ status offer Egyptian producers enough of an advantage—combined with Egypt’s own intrinsic competitive advantages (and disadvantages)—to enable them to compete successfully against other global suppliers and win market share in the United States?”

The target sectors are very large sectors with many products and product categories. Moreover, the sectors do not correspond neatly with product grouping categories in the Harmonized System of Tariff Codes (HS Code) categories used by the Customs authorities of the United States and the rest of the world. At the broad (4-digit) level of product grouping, the range of tariffs covering the products in the group is similarly broad, and therefore summarizing how useful QIZ status might be for the entire group of products is no simple matter. Most product tariffs are set at the 6, 8, or even 10-digit level – levels that carry a more precise product description. This complicates and increases the scale of the task exponentially. Egypt exports more than 1,300 engineering products alone, counted by the number of tariff lines imported to the United States from Egypt at the 8-digit level. One can sort the tariffs at the 8-digit level and the data on summary aggregations at the 4-digit level to find useful indications about the structure of tariffs in the category, but always with the caveat that the definitive answer depends on the actual 8- or 10-digit tariff classification assigned to the product by customs inspectors at the port of entry.

Even a slight change in how a product is produced or packaged can change the tariff classification and the applied tariff. The study examined the situation facing categories of products (at the 4-digit and 6-digit levels) and for a few specific products—defined at the 8-digit level—making it possible to use the data from the Harmonized System of Tariff Codes (HS Codes). Even if the posted tariff is not changed, the United States continues to negotiate and enter into FTAs or preferential trade agreements that allow duty-free or reduced duties on items from other countries. Egypt will increasingly compete with other countries’ duty-free access.

The TFP study team reviewed USAID studies and other studies of Egyptian exports—and QIZ exports specifically—along with U.S. and Egyptian data on exports to the United States and to the rest of the world. Unfortunately, each source uses different data collection methodologies and procedures for what should be the same information—U.S.-reported imports from Egypt and Egyptian-reported exports to the United States. Discrepancies in figures between QIZ exports from Egypt and QIZ imports into the United States are due to different source documents and are noted in each table. The team also interviewed principals with Egyptian firms, both QIZ exporters and non-QIZ exporters, and other market experts in Egypt and the United States.

The study team also studied the experience of Jordan, which has had the benefit of both a QIZ (since 1997) and an FTA (since 2005),⁵ and the experience of Morocco, which entered into an FTA with the United States in 2004.⁶ The experience of these two countries can give some indications about how their duty-free status has managed to attract investment or catalyze development in one or more of the industries in question.

⁵ With implementation phased in; full implementation in 2010.

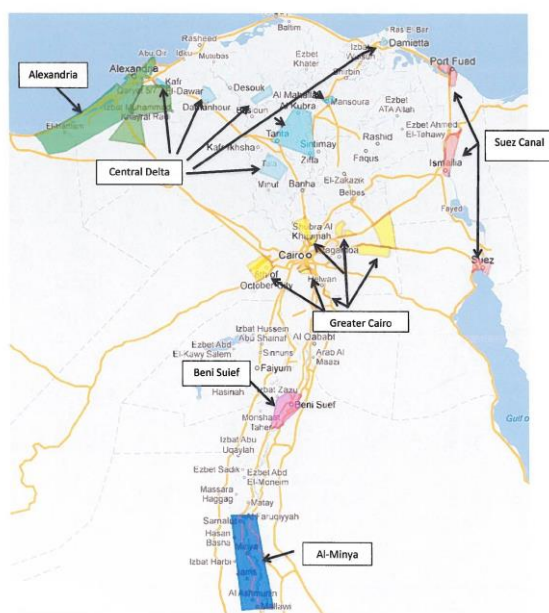
⁶ <https://ustr.gov/trade-agreements/free-trade-agreements/morocco-fta>

2. BRIEF HISTORY OF THE QIZ

The QIZ program in Egypt was first implemented in 2005; by 2011 exports had increased from \$250 million to approximately \$1 billion per year, then dropped to \$920 million in 2014. Egypt's overall exports to the United States more than doubled in the past 11 years, from \$925 million in 2000 to a peak of \$2.9 billion in 2012, before declining to \$1.4 billion in 2014 (Table 2-1, see end of this chapter). QIZs have been instrumental in spurring and sustaining Egyptian export levels. In 2014, a large majority of Egypt's exports entered the United States under the QIZ program (67 percent) and, even as growth in all Egyptian exports fluctuated between 2007 and 2011, QIZ export growth remained steady. And the growth in the products driving the increase in Egyptian exports—woven clothing, knitted clothing, and carpets—is largely attributable to QIZs.

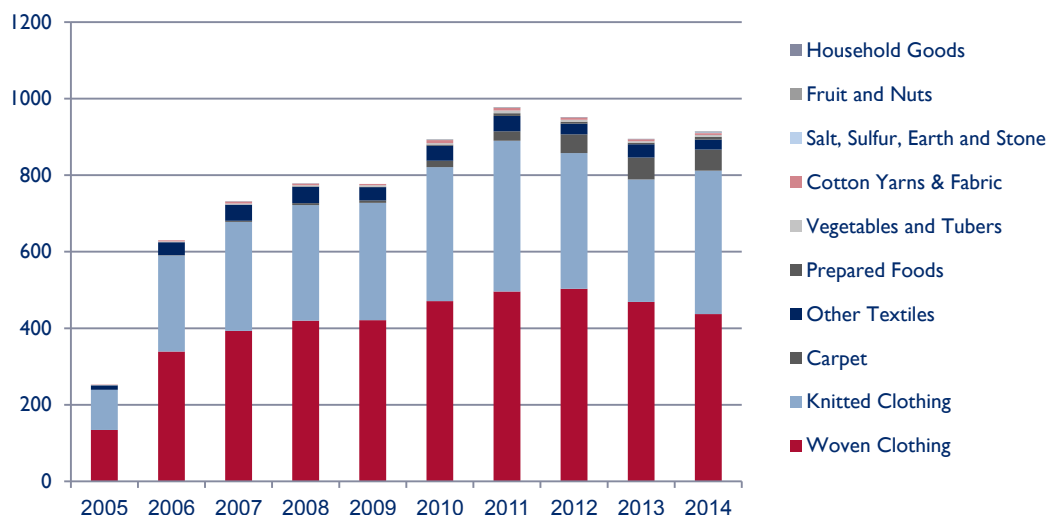
In 2005, the United States initially designated three QIZ areas in Egypt: Greater Cairo, Alexandria and Suez Canal (69FR4199); Central Delta, Expanded Greater Cairo, and Expanded Suez Canal (70FR69622). Two additional areas, in Beni Suef and Al Minya, were designated as QIZs in 2009 (74FR4482) (Figure 2-1).

Figure 2-1. Map of the Designated QIZs in Egypt



The initial QIZ designations applied to areas with the greatest concentration of Egyptian manufacturing capacity, especially private sector apparel producers with relationships with U.S. buyers. These firms had for some time been laying the groundwork for QIZs. Therefore, the Egyptian government and private sector were able to capitalize on QIZ benefits quickly without a lag for investing in new plants, equipment, labor, or market development.

Growth in QIZ exports from Egypt over the seven-year period since their establishment in 2005 is shown in Figure 2-2 and Table 2-2 (see end of section). Both show the rapid growth and predominance of woven and knit clothing in the mix of exported products.

Figure 2-2. Top 10 Categories of QIZ Exports to the United States, 2005–2014 (US\$ million)

- The first QIZs in Egypt began operating in 2005. Exports rose quickly to just over \$1 billion per year in 2011 but dropped to \$920 million (8.8 percent) by 2014.
- The first exporters to make extensive use of the QIZ program were in the ready-made garments (RMG) industry. Articles of clothing have been the dominant export ever since. In 2011, more than 95 percent of Egypt's QIZ exports consisted of RMG and household linens. By 2014, the share of RMG and household linens had decreased to 88 percent of QIZ exports.
- A small percentage of Egypt's QIZ exports is made up of food—processed, fresh, or otherwise prepared. Food exports from QIZs have increased 4 percent, but the share of total exports has increased only slightly from 1.5 percent to 1.7 percent.
- Approximately 250 companies of the 585 firms approved by Egypt as eligible for participation in the QIZ program export annually under the QIZ Protocol.
- For many private sector firms, in RMG and other sectors, the main factors and constraints governing their decisions to operate under and utilize QIZ status are business competitiveness issues (cost and market linkages) or the difficulties associated with complying with specific QIZ requirements for value-added of Egyptian and Israeli content.
- For some Egyptian firms, personal antipathy or public stigma may be attached to partnering directly with an Israeli firm to obtain Israeli-sourced inputs, but the QIZ unit at the Ministry of Industry, Trade, and Small and Medium Enterprises provides trade facilitation services to link Israeli suppliers to Egyptian producers at arm's length.

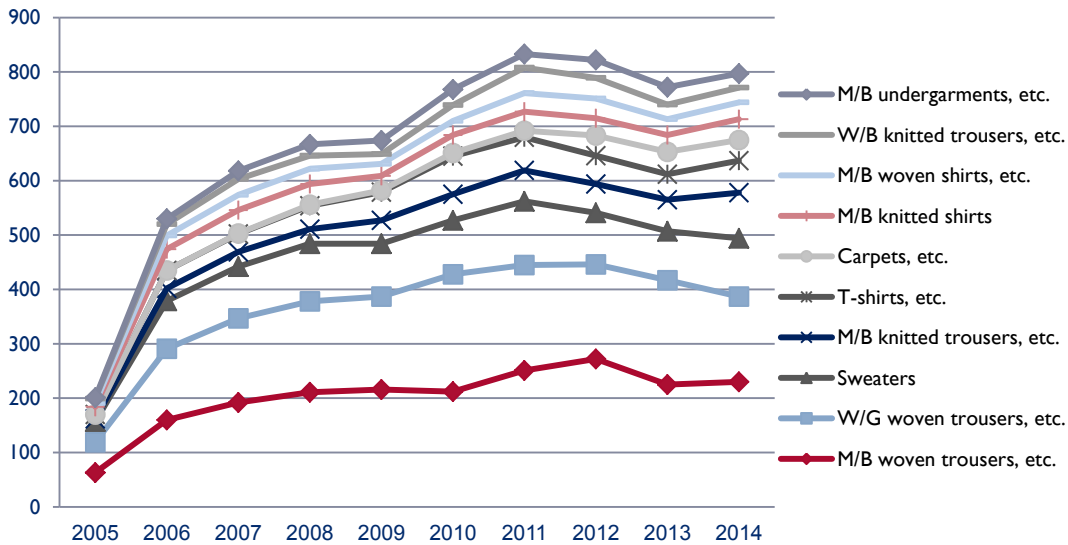
Creation of the QIZ program led to an initial surge in production and exports from Egypt in 2005 and 2006. In 2007 and 2008 growth was still remarkable, at 15–18 percent annually, but in 2009 QIZ exports declined 3 percent. QIZ exports rebounded somewhat in 2010, and by the end of 2011 were 15 percent above 2008 peak levels. From 2011 to 2014, exports decreased by almost 6 percent to \$920 million by 2014.

Upper Egypt does not offer a concentration of existing private sector apparel firms similar to that found in the first QIZs located in the Cairo, Delta and Suez Canal areas. In addition, Egypt has thus far not succeeded in diversifying the product composition of its QIZ exports, despite frequent urgings from the United States. Apart from RMG, the categories of exports to the US

have not seen significant growth. If Egyptian firms have not yet managed to generate significant new QIZ products in the relatively advanced business and manufacturing environs of existing QIZ zones, it would seem unlikely that they could do so quickly in the less developed area of Upper Egypt.

There has been a steady increase since 2005 in certain categories of apparel, most markedly for woven cotton trousers, but also for other types of trousers and manmade fiber knitted sweaters (Figure 2-3 and Table 2-3[see end of section]). In 2011, the top 10 products made up 70 percent of QIZ exports and 36 percent of total Egyptian exports to the United States. Since peaking in 2011, however, exports in woven cotton trousers have declined almost 15 percent, while many other categories have shown moderate or no growth.

Figure 2-3. Top QIZ Exports, by HS 4, 2000–2014 (2011 base year) (US\$ million)



An Upper Egypt QIZ designation would be expected to generate a similar profile of additional exports to the United States in apparel, textiles, and other products—with related increases in jobs and investment—as firms seek to capitalize on the region’s lower labor costs. Some owners have mentioned relocating from older QIZs to newer ones in Upper Egypt. Given the political difficulties of closing operations in Egypt, however, owners planning to invest in new QIZs will probably do so without liquidating ongoing operations elsewhere in Egypt. An increase in food-related products exported under QIZ is possible if expanded to agriculture-intense Upper Egypt, but the challenge of substantially transforming raw agricultural inputs to meet QIZ requirements could limit growth.

QIZs lend themselves to production of goods that would otherwise be subject to high import tariffs in the United States. This is particularly the case for products that are not eligible for GSP treatment, such as textiles and apparel, footwear, and luggage. Egyptian exports of RMG and textiles are subject to U.S. duties ranging from under 1 percent to over 30 percent,⁷ unless exported from a qualified QIZ exporter. Apparel and textile producers generally suggest that a

⁷ For example, the U.S. import duty on man-made fiber, knit sweaters—Egypt’s third-largest export category to the United States—is 32 percent.

good must be subject to a U.S. tariff of at least 10 percent for them to gain the necessary margin to compete with lower-cost producers in China and Bangladesh, and to offset the additional costs of including Israeli inputs. Representatives of Egypt's Chamber of Food Industries note that member companies have generally concluded that QIZs will be of limited value because most food products likely to be exported are subject to low U.S. tariffs and high testing costs.⁸

Proposals have been put forward for expansion of Egypt's QIZs. Experience from the 2009 expansion indicates that expansion can be expected to result in additional product exports and possibly additional diversification, depending on location. The expansion proposed in 2012 was expected to produce additional exports worth about \$150 million after two years, consisting mostly of clothing but also some food products, but the expansion was not implemented. Recently, the U.S., Egyptian, and Israeli governments have held discussions on renewing momentum to expand the QIZ program. At the time of the writing of this report, an agreement had not been reached.

⁸ U.S. duties on some food items are significant, e.g., the tariff on imports of dried onion and garlic powder (07122020) is 29.8 percent.

Table 2-1. Egypt's Exports to the United States, 2000–2014 (US\$ million)

| Import Program | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|------|------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| All other | 899 | 830 | 1,317 | 1,095 | 1,290 | 1,745 | 1,691 | 1,579 | 1,413 | 1,185 | 1,196 | 868 | 1960 | 657 | 413 |
| GSP | 26 | 22 | 24 | 32 | 38 | 65 | 70 | 61 | 57 | 45 | 51 | 49 | 60 | 71 | 67 |
| QIZ | 0 | 0 | 0 | 0 | 0 | 266 | 643 | 740 | 874 | 848 | 956 | 1,009 | 971 | 902 | 920 |
| Total exports | 925 | 852 | 1,341 | 1,127 | 1,328 | 2,076 | 2,404 | 2,380 | 2,344 | 2,078 | 2,203 | 1,926 | 2,991 | 1,630 | 1,400 |
| QIZ exports as a share of all Egypt exports | 0 | 0 | 0 | 0 | 0 | 12.8 | 26.7 | 31.1 | 37.3 | 40.8 | 43.4 | 52.4 | 32 | 55.3 | 66.7 |

Source: Compiled from tariff and trade data from the U.S. Department of Commerce and the U.S. International Trade Commission

Table 2-2. Top 10 QIZ Exports to the United States, by HS2 code, 2005–2014 (US\$ million)

| No. | HS 2 Code | Description | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|-----|-----------|-------------------------------|------|------|------|------|------|------|------|------|------|------|
| 1 | 62 | Woven Clothing | 134 | 339 | 393 | 420 | 421 | 471 | 496 | 503 | 469 | 437 |
| 2 | 61 | Knitted Clothing | 105 | 251 | 285 | 302 | 307 | 350 | 394 | 355 | 320 | 375 |
| 3 | 57 | Carpet | 0 | 1 | 3 | 5 | 6 | 17 | 25 | 49 | 57 | 55 |
| 4 | 63 | Other textiles | 12 | 34 | 42 | 43 | 35 | 39 | 40 | 28 | 35 | 26 |
| 5 | 20 | Prepared Foods | 0 | 0 | 0 | 1 | 1 | 3 | 7 | 5 | 4 | 7 |
| 6 | 07 | Vegetables and tubers | 1 | 2 | 3 | 3 | 4 | 4 | 7 | 5 | 4 | 5 |
| 7 | 52 | Cotton Yarns & Fabric | 1 | 3 | 5 | 4 | 3 | 8 | 7 | 6 | 5 | 5 |
| 8 | 25 | Salt, Sulfur, Earth and Stone | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 2 |
| 9 | 08 | Fruit and nuts | 0 | 0 | 0 | 0 | 0 | 1 | 1 | 0 | 0 | 2 |
| 10 | 94 | Household Goods | 0 | 0 | 1 | 1 | 0 | 1 | 1 | 1 | 1 | 1 |
| | | All Other | 12 | 9 | 7 | 92 | 67 | 60 | 30 | 16 | 4 | 4 |
| | | Top 10 QIZ exports total | 253 | 630 | 732 | 779 | 777 | 894 | 978 | 952 | 895 | 920 |

Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitic.dataweb.gov

Table 2-3. Top 10 HS4-Category Exports to the United States, 2000–2014 (US\$ million)

| No. | HS 4 Code | Description | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|----------|-----------|----------------------------|------|------|------|------|------|------|------|------|------|------|
| 1 | 6203 | M/B woven trousers, etc. | 63 | 160 | 192 | 211 | 216 | 212 | 251 | 272 | 225 | 230 |
| 2 | 6204 | W/G woven trousers, etc. | 56 | 131 | 155 | 167 | 171 | 216 | 194 | 174 | 192 | 157 |
| 3 | 6110 | Sweaters | 38 | 88 | 95 | 106 | 97 | 99 | 117 | 95 | 90 | 107 |
| 4 | 6103 | M/B knitted trousers, etc. | 5 | 23 | 27 | 27 | 43 | 48 | 57 | 53 | 58 | 84 |
| 5 | 6109 | T-shirts, etc. | 8 | 33 | 33 | 43 | 52 | 70 | 61 | 52 | 47 | 59 |
| 6 | 5703 | Carpets, etc. | 0 | 0 | 1 | 2 | 3 | 6 | 12 | 37 | 41 | 38 |
| 7 | 6105 | M/B knitted shirts | 14 | 39 | 43 | 38 | 27 | 33 | 35 | 32 | 31 | 38 |
| 8 | 6205 | M/B woven shirts, etc. | 7 | 25 | 28 | 28 | 22 | 26 | 34 | 36 | 29 | 31 |
| 9 | 6104 | W/G knitted trousers, etc. | 8 | 21 | 29 | 24 | 18 | 29 | 47 | 38 | 27 | 27 |
| 10 | 6107 | M/B undergarments, etc. | 2 | 10 | 15 | 21 | 25 | 29 | 25 | 33 | 32 | 26 |
| Subtotal | | | 201 | 530 | 618 | 667 | 674 | 768 | 833 | 822 | 772 | 797 |

Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitic.dataweb.gov

3. TRADE VOLUMES IN PERSPECTIVE

Egypt’s nearly \$1 billion in QIZ exports in 2014 made up 81.5 percent of the country’s total exports to the United States (see Table 3-1). With RMG accounting for close to 90 percent of total QIZ exports, the QIZ program is obviously of chief importance to Egyptian producers in these sectors.⁹

Table 3-1. Summary of Egypt’s Exports to the World and United States

| Destination | Egypt Exports (US\$ million) | | | Exports to U.S. as % of Total Exports | | Imports from Egypt as % of Total U.S. Imports | |
|--------------------------|------------------------------|--------|--------|---------------------------------------|-------|---|--------|
| | 2009 | 2011 | 2014 | 2011 | 2014 | 2011 | 2014 |
| World, Total | 24,182 | 31,582 | 26,812 | 6.30% | 4.21% | 0.90% | 0.06% |
| United States, Total | 1,633 | 1,819 | 1,129 | | | | |
| United States, under QIZ | 848 | 1,099 | 920 | 3.48% | 3.43% | 0.05% | 0.039% |

Note: There are data discrepancies between USITC import data reported in Table 2-1 and UN Comtrade Data reported in Table 3-1. The authors attempted to use a consistent data source in each table and the most reliable for the type of comparison being conducted.

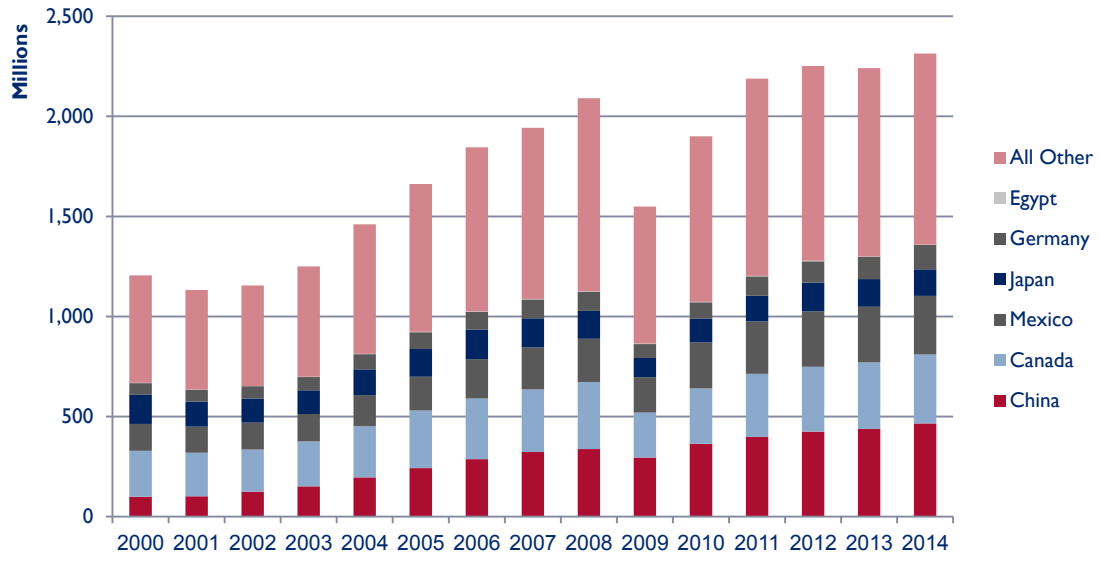
Source: UN Comtrade Data and U.S. Department of Commerce Data

Compared to other export destinations, however, the United States is not a large market for Egyptian exports. Egypt’s total exports (QIZ plus all other) to the United States accounted for 4.2 percent of its exports to the world in 2014, down from 6.3 percent in 2011 (Figure 3-1). And Egypt’s QIZ exports to the United States represented only 3.4 percent of total Egyptian exports in 2014, slightly up from 3.3 percent in 2011. Egypt’s most significant trade partners are Italy, India, and Saudi Arabia, which together account for 22 percent of Egypt’s exports.

Moreover, when compared to the value of all goods imported into the United States in 2014 (\$2.3 trillion), the share of U.S. imports that come from Egypt’s QIZs is miniscule. Egypt’s total exports to the United States in 2014 (\$1.1 billion) accounted for 0.06 percent of all U.S. imports that year, and imports under the QIZ preference program were two-thirds of that (0.039 percent)—less than one-half of 1 percent. From the U.S. perspective, in the apparel sector, China, Vietnam, Indonesia, Mexico, and Bangladesh are the five largest suppliers of apparel, and Egypt ranks 17th. Figure 3-1 shows the top five suppliers to the U.S. market, plus Egypt and all other suppliers.

⁹ RMG is used here as the sum of HS codes for woven and knitted clothing. Household linens are mainly other textiles, sheets and towels, excluding carpets and rugs.

Figure 3-1. Major Suppliers of Apparel to the U.S. Market, 2005–2014 (US\$ million)



Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitic.dataweb.gov

4. U.S. TARIFFS OVERVIEW

The first thing to note about providing preferential tariff treatment to Egyptian exports to the U.S. market is that except for a few product categories, U.S. tariffs are already low and have tended to decrease over time. This trend reduces the absolute and relative advantage of any preferential treatment, including tariff-free access. The second thing to note is that even for products with U.S. tariffs that might seem significant (>20 percent) the United States has entered into FTAs and other agreements with a number of countries. For each FTA, with some variation in value-added minimums and rules-of-origin requirements, export firms in that favored nation can compete with Egyptian QIZ exports on a duty-exempt footing. As of this writing, the United States had signed 14 FTAs with 20 countries.

The World Trade Organization (WTO) tracks tariffs in its member countries. The 2014 WTO report on the United States indicates less than 3.2 percent of agricultural items imported into the United States (at the 8-digit HS code level) were subject to a tariff higher than 15 percent. Of nonagricultural goods, 3.9 percent were subject to such a tariff rate. More than 40 percent of agricultural products and almost 49 percent of nonagricultural products entered the United States tariff free in 2012 (see Table 4-1 at the end of the chapter).¹⁰

This does not mean there are no examples of U.S. imports subject to high tariffs. Major product groups entering the United States are still subject to significant tariffs and/or quotas, including dairy products, sugar and confectionary products, raw agricultural products, leather, footwear, and RMG. The high tariffs that continue to be applied to RMG are one reason RMG has been so successful in Egypt's QIZs.

To evaluate the potential tariff benefit afforded by QIZ status for an Egyptian exporter, one has to know the exact tariff that would be applied to the product made in the QIZ. This is difficult to do in the abstract, because tariffs are applied using a very specific determination of the material composition at a highly defined level of product. There are thousands of such codes, each corresponding to a different product description; for example:

- HS Code 6403.99.6075—corresponds to “Men’s Sandals or Flip Flops with leather uppers and plastic or rubber sole”—the applicable tariff is 8.5 percent ad valorem.
- HS Code 6403.20.00—corresponds to “Sandals or Flip Flops with straps for the instep and big toe”—can enter the U.S. tariff-free.

¹⁰ World Tariff Profiles, 2014. World Trade Organization.
https://www.wto.org/english/res_e/publications_e/world_tariff_profiles14_e.htm

- HS Code 6404.20.6060—corresponds to a “Woman’s shoe, with outer soles of leather or composition leather and textile uppers, not otherwise specified”—the applicable tariff is 37.5 percent ad valorem.

These very specific product descriptions can make it difficult for exporters to be certain of the applicable tariff for their products. It is not unusual for a firm or country to ask U.S. Customs for guidance or a preliminary tariff ruling before attempting to export.¹¹ Although identifying the specific tariff for leather accessories and garments is relatively straightforward, for other categories such as footwear and processed foods identifying the specific category is difficult. Processed foods are addressed in 24 HS chapters, making it challenging to come to a conclusion about tariffs affecting products in this sector that might benefit from QIZ’s tariff-free access to the United States. The next section attempts to bridge the gap between the thousands of individual products (8-digit HS codes) and larger categories that come close to corresponding to the target product categories under consideration in this study.

¹¹ An exporter can use a tariff calculator to determine what duties will be applied to the product they wish to export to a certain country such as the United States. A commercial example is the Duty Calculator (<http://www.dutycalculator.com/compare-plans/nr-ni/>).

Table 4-1. U.S. Tariff Structure (WTO), 2013 Tariff Lines and Import Values (%)

| Frequency Distribution | | Duty-free | 0<=5 | 5<=10 | 10<=15 | 15<=25 | 25<=50 | 50<=100 | >100 | NAV |
|---------------------------------|------|-----------|------|-------|--------|--------|--------|---------|------|------|
| AGRICULTURAL PRODUCTS | | | | | | | | | | |
| Final bound | | 30.2 | 44.3 | 13.1 | 4.3 | 3.0 | 1.6 | 0.4 | 0.5 | 41.3 |
| MFN applied | 2013 | 30.8 | 45.8 | 12.4 | 4.6 | 3.0 | 1.5 | 0.4 | 0.8 | 41.4 |
| Imports | 2012 | 41.0 | 36.2 | 12.5 | 7.0 | 1.7 | 0.7 | 0.6 | 0.2 | 4.0 |
| NONAGRICULTURAL PRODUCTS | | | | | | | | | | |
| Final bound | | 47.4 | 26.8 | 17.1 | 4.9 | 1.9 | 0.5 | 0.0 | 0 | 3.2 |
| MFN applied | 2013 | 50.6 | 24.9 | 16.3 | 4.7 | 1.7 | 0.4 | 0.0 | 0 | 3.1 |
| Imports | 2012 | 48.9 | 40.2 | 6.2 | 0.9 | 3.1 | 0.7 | 0.0 | 0 | 0.0 |

Note: NAV means "non ad-valorem".

Source: WTO trade statistics.

5. SELECTED PRODUCT GROUPS

This section looks at the four product categories and the possible benefit of QIZ status for potential exporters in each, as well as other factors influencing the likelihood of exporting successfully to the United States. The sectors specified in the SOW (footwear, leather accessories, processed foods, and light manufactured products) do not always correspond neatly to specific tariff code categories used by U.S. Customs. In this report, we selected the most appropriate categories for gauging likely tariffs for the products in the specified sectors.

To put Egypt's experience with the QIZ program in perspective, we also compare the experience of Jordan and Morocco and their trade preference programs. Jordan has both an FTA and a QIZ program with the United States, and Morocco has an FTA. For leather footwear, the Jordanian experience is particularly relevant because the early expectations for the Jordanian QIZ program were similar to those for Egypt.

LEATHER FOOTWEAR

Egypt

After the establishment of QIZ in Egypt, it was expected that RMG would be the first industry to take advantage of the arrangement. Egypt was already an established producer and exporter of RMG with long-established buyers in the United States, with exports subject to the multifiber quota system that expired in 2005. Moving from the previous quota system to the QIZs did not require new investment or new marketing arrangements with buyers in the United States: Egypt had established market share, and the physical boundaries for QIZs included most of the factories in Egypt making RMG for export.

Early expectations for the QIZ program were that success with RMG exports would lead to new investment and that exports would increase and diversify into footwear products with similar production processes and overlap in the market linkages in the United States. These expectations were not realized in Egypt or Jordan (which had a similar QIZ program), for reasons that other studies have sought to explain. Most of these studies have concluded that shoe manufacturing is more specialized and more challenging than RMG and more dependent on achieving economies of scale. As a result, shoe manufacturing has been concentrated in East Asia, particularly in China—the world's largest consumer and exporter of shoes. China's enormous domestic market enabled manufacturers to invest in and benefit from larger factories than most countries had established. In turn, large factories and economies of scale allowed China to dominate the global market in inexpensive, low-quality shoes—flooding markets of many countries and sending local footwear manufacturers into decline. China's competitiveness increasingly suffers from rising labor costs, but the industry still retains

significant cost advantages over manufacturers in other countries. Chinese factories have used this extended period of market dominance to upgrade manufacturing quality, contract with high-end global brands, and dominate most aspects of the industry.

Egypt does export some leather shoes. Table 5-1 (see end of the chapter), shows the six largest categories of Egypt's exports of leather footwear products in 2014 arranged according to 4-digit HS category codes with brief descriptions. Most of Egypt's exports fall under HS 6403 Footwear with leather upper. In 2014, Egypt exported more than \$10 million of leather footwear, including \$293,000 to the United States. The maximum tariff that U.S. customs applies to this category of product would be 10 percent, and many items could enter for a lower duty. For the bulk of Egypt's leather footwear exporters, striving for QIZ status would not be an attractive strategy, considering that complying with Israeli content minimums and the with QIZ reporting requirements and audits may cost more than the waived tariff benefit of 10 percent. In addition, countries close to the U.S. market, such as Mexico, also enjoy tariff-free access to the U.S. market.

Egypt also exports other footwear items, included in Table 5-1 (see at the end of the chapter). Some products in these categories could be subject to tariffs in the United States in the range of 26 percent to 48 percent, an amount that in the abstract could be a sufficient incentive for many firms and even investors. Yet Egypt exports few or no products in these categories to the United States and less than \$2 million to all other non-U.S. markets.

Other information confirms that leather footwear is an industry in decline in Egypt, as it is in most other countries. More than 75 percent of raw materials, including hides, have to be imported because hides tanned in Egypt will not pass the sanitary, environmental, and consumer safety regulations in the U.S. or EU. Egyptian tanneries, most located in Cairo, employ poor technical methods of chrome tanning that leave high residual levels of Chromium III and VI (hexavalent chromium) in finished products. The tanneries flush their dangerous chemical waste directly into the Nile. Few have moved out to the model tannery area (*al-Robaki*) built with technical assistance from Italy in the suburbs of Cairo. Egypt also lacks modern manufacturers or suppliers of other footwear-making materials and equipment such as quality rubber or plastic (polyurethane) for soles or the molds (lasts) that modern shoemaking requires. Although businesses report skilled or unskilled labor is not hard to find, there are few established higher educational, vocational, or practical labs to increase technical capacity across the industry.

Jordan

Jordan has a QIZ agreement with Israel and the U.S. similar to Egypt's QIZ program. In October 2000, Jordan entered into a free trade agreement (FTA) with the U.S. that was slowly phased in until fully implemented in 2010.¹² A few years after the FTA was signed, a study was conducted to look at the prospects of the footwear industry in Jordan. "Global Footwear Analysis and Jordan" used data from 2000 to 2002 and inspections of Jordanian footwear factories to conclude that Jordan could take advantage of its FTA with the United States in

¹² In 2009, QIZ products still accounted for more than half of Jordanian exports to the United States but the QIZ share has declined in favor of the FTA. (<http://ustr.gov/trade-agreements/free-trade-agreements/jordan-fta>).

footwear only if it embarked on a five-year development plan with European partners to upgrade tanneries and footwear factories, set up a special training program, and implement tariff protection legislation that would keep Chinese-made shoes out of the Jordanian market for at least five years until the industry could develop. The study estimated that Chinese-made women's shoes were entering Jordan after paying 100 percent or more in tariff duties were still being sold at two-thirds the cost of making the same shoe in Jordan.¹³ And Jordan's experience is not unique. Many countries, including Egypt, have seen their domestic footwear manufacturers decimated by cheap Chinese imports.

Potential Growth for Egypt QIZ Exports

This experience does not mean there is no footwear product that could take advantage of the QIZ program, but leather footwear, specifically, does not appear to be a promising product category for diversification. A more interesting product might be house slippers made of textile uppers with rubber soles. Egypt would have to import the rubber soles but might have an advantage using soft Egyptian cotton for the upper parts of the slipper. The U.S. customs tariff on such slippers is currently 37.5 percent ad valorem. This tariff could be attractive to a U.S. importer or retailer. A reliable relationship with a U.S. buyer would be needed before investing in this type of new product. Such a relationship might be possible to cultivate for textile footwear that matched household linens. An importer or retailer in the United States currently paying 37.5 percent tariff duty on every pair of imported house slippers might be interested in examining the option of sourcing production that qualifies for the QIZ tariff exemption.

LEATHER ACCESSORIES

Egypt

Table 5-3 (see at the end of the chapter) shows Egypt's global exports of leather accessories for its three largest product categories in 2014. In that year Egypt exported less than \$3 million in all three categories combined, and 94 percent of those exports came under the HS code 4205, which covers a wide range of articles of leather or leather composition not elsewhere specified. Products in this category would be subject to a 4.9 percent tariff by U.S. customs, but almost none of Egypt's exports in this category go to the United States. Most of these items are made under agreements with European manufacturers in Italy or Spain.

There are two leather accessory products that Egypt exports to the world that are subject to a tariff rate above 10 percent when exported to the United States—leather bags or trunks, and leather apparel and accessories. The same health, consumer safety, and environmental constraints facing potential diversification into leather goods outlined on page 15, however, would apply to these products as well. In addition, Egyptian producers lack market linkages to U.S. buyers to sell or tailor their products to the U.S. marketplace.

¹³ Source: <http://www.scribd.com/doc/86907358/Glbal-Footwear-Analysis-and-Jordan-1#scribd>.

Morocco

Leather producers in Morocco have strong commercial ties to high-fashion houses in Italy, Spain, Portugal, and elsewhere in the European Union. They have provided advice, fashion guidance, and other technical assistance to producers in Morocco, frequently under production agreements that call for most of the product to be shipped to the European partner.

Morocco signed an FTA with the United States in 2004 that entered into effect in January 2006. In 2014, Morocco's global exports of leather products were \$71 million, of which 1 percent went to the U.S. market. An early expectation of the extension of tariff-free trade access to Morocco was an increase in the leather accessories exported to the U.S. marketplace. As shown in Table 5-4 (see end of the chapter), the growth in Morocco's leather accessory exports to the U.S. market underperformed the growth of imports of leather accessories into the U.S. market from all countries on average. A more rigorous analysis of competitiveness constraints specific to Morocco and possible regression analysis could determine attributable causes; on its face, however, there seems no clear indication of a positive impact of tariff-free access on the Moroccan leather industry—a lesson for Egypt under the QIZ program.

LIGHT MANUFACTURING—ENGINEERED PRODUCTS AND ELECTRONICS

Egypt is a significant exporter of light manufacturing products. More than 500 Egyptian firms are members of the Egyptian Engineered Products Export Council, which represents producers and exporters making everything from insulated wire and cable to auto parts, household appliances, flat-screen televisions, lighting fixtures, and air conditioners.

Egypt exported more than \$1.8 billion of products in HS chapters 84, 85, and 87 in 2014, with most of the exports falling into the 11 product code categories shown in Table 5.1 at the end of this section.

In the same year, Egypt's total exports in these categories to the United States were less than \$2.2 million, almost all in insulated wire and cable, which is subject to a U.S. customs duty of 5.3 percent. For most other items in the light manufacturing category, the U.S. duties are even smaller—only 1.8 percent for refrigerators and freezers, 2.2 percent for air conditioners. Such low tariff rates mean that Egyptian producers and exporters of these products have little to gain from pursuing QIZ status. In addition to the added cost of partnering with Israeli partners to get the minimum required Israeli content in the product, there would be the additional costs of reporting and compliance. More significant, though, would be the cost of retooling and reengineering their own production processes to meet the specifications and standards required in the U.S. market.

Although high-quality Egyptian manufacturers can meet the standards necessary to obtain the European mark (CE or *Conformité Européene*) needed to sell products in the EU, few make products certified by Underwriters Laboratories (UL), needed to sell in the U.S. market. Many firms choose not to invest in UL certification because they do not have connections to U.S. buyers to justify the investment. In addition, Egypt's own electrical system and appliances are compatible with those in the European Union but not with those in the United States. A similar problem would face many of Egypt's auto parts makers, which are tooled to the metric system and European-model vehicles rather than U.S. models. The investment required would be considerable, and the gains from exporting to the United States under the QIZ program

would be marginal at best. The incompatibility of U.S. specifications and Egypt's proximity to the European market are probably the main reasons there are so few exports from Egypt to the United States in this category.

PROCESSED FOOD PRODUCTS

Processed food products are one area of exports where QIZ status seems to be attractive to U.S. importer/buyers and eventually customers. In general, fresh food products, which face high U.S. tariffs and for which duty-free entry would be attractive, are ineligible for QIZ status because they do not meet requirements for substantial transformation and an Israeli input minimum. Processed foods also face the burden of proving to U.S. Customs that they have undergone substantial transformation, and there have been significant disputes over this issue, including a recent one regarding canned artichokes exports from Egypt to the United States.

For market and logistic reasons, Egypt will generally find the European Union to be a better (higher margin, lower transport cost) market for its fresh food products than the United States. EU markets are only hours away from Alexandria. The United States, however, is an attractive market for certain processed food products with a high-enough tariff barrier. There is also the attraction of serving the ethnic food market, which is growing in the United States. Unlike footwear and leather accessories, retailers and end markets for food products are less concentrated and easier to access for Egyptian exporters.

The tariff advantage of QIZ status for processed food exporters is more difficult to determine than for other sectors discussed in this report. Several products are subject to a flat rate rather than ad valorem duties, and ad valorem rates are typically higher than the rates for light manufactured products, electronics, or even some footwear.

Table 5-6 also shows that Egypt's global exports in this category are in the billions of dollars. The table stops at the 17th-largest category, which still amounted to more than \$44 million in 2014. Only a small share of these exports goes to the United States. The first seven products listed in Table 5-6 are exported to the Middle East and EU destinations (mostly to Italy) for consumption and re-export. The lack of exports to the United States is partially due to the proximity of the EU market, but there is another potential constraint: U.S. phytosanitary standards and regulations.

U.S. phytosanitary standards for food imports are stringent, and imports from Egypt are often stopped at the border for pests, pesticide residue, or failure to meet other standards. Egyptian importers and exporters cannot operate successfully with the risk that entire shipments of product will be stopped from entering for health or safety reasons. Egyptian exporters may not be able to control poor agricultural practices such as excessive use of insecticides that sometimes have prevented Egyptian olive products from passing U.S. FDA inspections. For example, the closeness of neighboring Egyptian farms and shared irrigation water can lead to contamination from farmers using poor practices (such as overuse of sprayed insecticides). Egypt is only starting to engage in the processes of farm-to-fork traceability that will be required in the future by U.S. and EU importers. Investments to control quality and establish traceability and demonstrations of substantial transformation of food within the QIZ will be needed.

Yet despite these challenges, some firms have managed to penetrate the U.S. market. Egyptian firms exported \$14 million of frozen vegetables (HS 0710) to the United States in 2014 and almost \$10 million worth of fruit and vegetable juices. The U.S. firm H.J. Heinz has built a multimillion dollar bottling and canning operation in Egypt. Egypt's leading manufacturers of juices have adopted state-of-the-art processing and packaging.¹⁴ In addition, informal reports indicate that Israeli partners feel positive about the prospects of partnering with more processed food enterprises in Egypt's QIZs, possibly supplying canning and packaging materials for exports.

The ultimate economic impact on poverty reduction is likely to be much greater from success in the processed food export category than in the other categories examined in this report.

Finally the potential economic development impact should be taken into consideration. An Egyptian-grown and -processed food export will have far greater backward linkages and multiplier advantages for the Egyptian economy than do leather shoe exports, for which Egyptian manufacturers import probably more than 75 percent of needed materials. The ultimate economic impact on poverty reduction is likely to be much greater from success in the processed food export category than in the other categories examined in this report.

IMPACT ON U.S. JOBS

Earlier studies have pointed out that imports of RMGs into the United States from Egypt would not have a measurable impact on U.S. employment because very few RMGs are produced in the United States today. Increased exports from Egypt would come at the expense of exports from China or other East Asian sources but would not affect U.S. employment. The same could be said for leather footwear, another industry that most U.S. producers have exited. Although it is not easy to make a general statement about light machinery or foodstuffs without a more detailed look at the specific product and the quantities that would be expected to enter the U.S. market from Egypt—an analysis that would be product specific and is outside the scope of the current study—we suspect the minimal share of Egyptian exports in the U.S. import market (0.06%) suggest limited to no impact on U.S. jobs of export growth in these sectors.

TRANSPORT AND LOGISTICS

The statement of work for this assignment included a request to:

Provide market information on products identified as offering the greatest tariff benefit, including current suppliers, their respective market shares in the U.S. market, and average CIF prices in the United States. Provide estimates of FOB prices of these products at a reference port in Egypt and compare these estimates to equivalent wholesale prices in Egypt in the same reference port.

The purpose of this request is to reveal Egypt's competitive position in these products and inform how easily or difficult it will be to enhance competitiveness. As this report's

¹⁴ See www.juhayna.com

methodology combines a desk-study tariff analysis with a rapid one-week qualitative competitiveness assessment, this report describes the product associated prices of Egypt's competitive position and how further, more quantitative and rigorous study, could reveal the difficulty to enhancing competitiveness in Egypt.

In this section the authors select a few specified product groups at the 4-digit HS level, and, using the U.S. International Trade Center's data, cite the Customs value (hereafter used as a proxy for Free on Board or FOB) and cost, insurance, and freight (CIF) value for U.S. imports from Egypt. But these values reflect products that by definition Egyptian exporters and U.S. importers have already judged to be competitive, i.e., sellable in the U.S. marketplace. For products that are not being imported to the United States from Egypt, additional research using value chain methodology and incorporating market surveys of Egyptian wholesale prices should be considered to address specific product competitiveness.

The comparison of wholesale prices to FOB prices in Egypt should be able to reveal domestic or logistical constraints reducing the competitiveness of Egyptian products within domestic distribution systems. Over the course of several interviews with enterprises in Egypt, no firms identified the domestic distribution system as a problem for exporting. In fact, several firms said exporting was relatively simple, cheap, and quick. The inexpensive cost of internal trucking, availability of export facilitation firms, and familiarity with export requirements were cited. However, several firms indicated the high cost of importing Israeli inputs limited the cost competitiveness of their final products. Specifically, the high cost of trucking products from Israeli factories to ports for export and the high cost of freight from the port of Haifa to Alexandria were cited (the latter may be due to limited seaborne trade between the countries). Most firms listed the high cost and difficulty associated with importing raw inputs into Egypt from any country as an impediment to price competitiveness.

The comparison of FOB and CIF prices for selected products exported from Egypt can indicate if there are constraints in the international freight and insurance services facing Egyptian exporters. A detailed market survey at the main ports of Egypt could reveal the exact FOB prices associated with these selected products; however, in lieu of these definitive prices, the customs value, appraised at import by U.S. Customs, can be used as a proxy. The difference between Customs value and CIF prices are the cost of freight and insurance. Interviews with freight forwarders and exporting firms in Egypt revealed that few to no firms use insurance when exporting overseas. A freight forwarder indicated that vessels maintain umbrella insurance that covers cargo lost in a sinking or tossed overboard to rebalance ballast. It is assumed this insurance cost is included within freight costs.

In Tables 5-7 to 5-10 at the end of the section, the customs value and the CIF prices are compared for the four sectors reviewed for this report. It should be noted that a more detailed value chain analysis for each product could reveal why freight costs differ, e.g. the difference between refrigerated, bulk, and specialized shipping. In Table 5-7, most processed food exports from Egypt appear to have low freight costs as a percentage of assessed customs value between 4 and 16 percent, with bulk goods the cheapest and juices, jams, jellies, and marmalades the most expensive. In Table 5-8, footwear with an upper of leather has a low freight cost of 5 percent of customs value. In Table 5-9, leather accessories have relatively high freight costs, ranging from 12 to 18 percent, but this could be related to a low trade volume—less than \$30,000 overall. In Table 5-10, the selected light manufacturing products have the lowest freight costs overall with all at or below 5 percent. Overall, firms interviewed

found the cost of freight from Egypt to the United States to be cheaper than for imports from the United States because of the prevailing trade deficit.

The rapid assessment conducted in the field in May 2015 and the price comparison in the abovementioned tables show that domestic and international transport and logistics do not appear to be a significant constraint for Egyptian exporters. A more rigorous quantitative analysis could reveal a more definitive understanding of Egypt's competitiveness in the U.S. market compared to those of other competitors.

METHODOLOGICAL LIMITATIONS

This report has a narrow methodological focus on the potential for QIZ export diversification of four predetermined sectors. As an update to a 2012 QIZ report, this report hews closely to the design and structure of the previous report. When possible, the authors incorporated the insights on sectoral competitiveness gained from a few brief interviews with key industry insiders carried out in May 2015. With limited time because the project was ending, predetermined sectors, a single destination market (United States), and program constraints (QIZ protocol), this report does not address all exports or the overall potential for Egypt's export diversification, but only the potential of these four sectors to represent a greater share of Egyptian exports to the United States under the QIZ program. In addition, this report reflects the current situation in Egypt and does not attempt to address how to diversify exports or increase the competitiveness of these sectors in the future.

Table 5-1. Egypt's Exports to the World and the United States, by HS4, 2014 (US\$ 000)

| Product code | Product Description | Exports to the World | U.S. Imports from Egypt | U.S. Imports from Egypt QIZ | QIZ Imports as % of All U.S. Imports from Egypt | Maximum U.S. Applied Tariff |
|--------------|--|----------------------|-------------------------|-----------------------------|---|-----------------------------|
| 6403 | Footwear, upper of leather | \$10,593 | \$375 | - | 0% | 10% |
| 6402 | Footwear nes, outer soles and uppers of rubber or plastics | \$549 | - | - | N/A | 37.50% |
| 6405 | Footwear, nes | \$401 | - | - | N/A | 12.50% |
| 6406 | Part of footwear; removable in-soles, heel cushion etc. | \$344 | - | - | N/A | 26.20% |
| 6404 | Footwear, upper of textile mat | \$122 | - | - | N/A | 48% |
| 6401 | W/p foot, outer sole/upper of rubber/plastic upper not fixed to sole nor assembled | \$76 | - | - | N/A | 37.50% |

Note: There are data discrepancies between USITC import data reported as U.S. Imports from Egypt and UN Comtrade Data reported as Exports to the U.S. The authors attempted to use a consistent data source in each table and the most reliable for the type of comparison being conducted.

Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitic.dataweb.gov. Export data to the world comes from COMTRADE Trademap.

Table 5-2. Egypt, Jordan, and Morocco's Exports to the United States, 1996–2014 (US\$ million)

| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|---------|------|------|------|------|------|------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Egypt | 718 | 820 | 707 | 703 | 925 | 852 | 1,341 | 1,127 | 1,328 | 2,076 | 2,404 | 2,380 | 2,344 | 2,078 | 2,203 | 1,926 | 2,991 | 1,630 | 1,400 |
| Jordan | 25 | 26 | 16 | 31 | 73 | 229 | 412 | 673 | 1,093 | 1,267 | 1,421 | 1,333 | 1,139 | 924 | 974 | 1,060 | 1,155 | 1,196 | 1,354 |
| Morocco | 255 | 300 | 352 | 414 | 456 | 453 | 410 | 396 | 545 | 470 | 546 | 626 | 880 | 467 | 686 | 994 | 934 | 999 | 1,010 |

While the specific circumstances surrounding the spike in exports in 2012 is unclear, closer inspection of COMTRADE data indicates this spike was mostly caused by, in order of impact, largest to smallest, the following sectors: fuels, fertilizers, iron and steel, apparel, earths and stone, vehicles, preparations of vegetables and fruits, man-made staple fibers, and miscellaneous edible preparations.

Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitic.dataweb.gov. Export data to the world comes from COMTRADE Trademap.

Table 5-3. Egypt's Top Exports of Leather Accessories, 2014 (US\$ 000)

| Product code | Product label | Exports to the World | U.S. Imports from Egypt | U.S. Imports from Egypt QIZ | QIZ Imports as % of All U.S. Imports from Egypt | Maximum U.S. Applied Tariff |
|--------------|---|----------------------|-------------------------|-----------------------------|---|-----------------------------|
| 4205 | Articles of leather or composition leather, nes | \$2,679 | \$11 | - | 0% | 4.90% |
| 4202 | Trunks, suit-cases, camera cases, handbags | \$173 | \$16 | \$5 | 31% | 20% |
| 4203 | Articles of apparel & clothing accessories, of leather or composition leather | \$26 | \$5 | - | 0% | 14% |

Note: There are data discrepancies between USITC import data reported as U.S. Imports from Egypt and UN Comtrade Data reported as Exports to the U.S. The authors attempted to use a consistent data source in each table and the most reliable for the type of comparison being conducted.

Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitic.dataweb.gov. Export data to the world comes from COMTRADE Trademap.

Table 5-4. Leather Accessory Exports from Morocco, 2006–2014 (US\$ 000)

| 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|------------|------------|------------|-----------|------------|------------|------------|------------|------------|
| MOROCCO'S EXPORTS TO THE UNITED STATES | | | | | | | | | |
| 1,653 | 1,419 | 1,307 | 832 | 663 | 1,199 | 1,553 | 1,471 | 766 | 745 |
| % change y/y | -14% | -8% | -36% | -20% | 81% | 30% | -5% | -48% | -3% |
| U.S. IMPORTS FROM WORLD | | | | | | | | | |
| 9,386,395 | 10,145,022 | 10,711,610 | 10,786,934 | 8,556,312 | 10,523,582 | 11,718,948 | 12,721,088 | 13,418,604 | 13,870,467 |
| % change y/y | 8% | 6% | 1% | -21% | 23% | 11% | 9% | 5% | 3% |
| MOROCCO'S EXPORTS TO WORLD | | | | | | | | | |
| 63,981 | 63,870 | 59,462 | 64,343 | 59,901 | 65,015 | 63,223 | 67,396 | 65,980 | 70,580 |
| % change y/y | 0% | -7% | 8% | -7% | 9% | -3% | 7% | -2% | 7% |
| MOROCCO'S EXPORT SENSITIVITY BEFORE AND AFTER THE U.S.-MOROCCO FTA | | | | | | | | | |
| | -2 | -1 | -52 | 1 | 4 | 3 | -1 | -9 | -1 |

A negative number indicates Morocco underperformed in leather accessory exports to the U.S. compared to other countries, while a positive number indicates Morocco over performed.

Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitic.dataweb.gov. Export data to the world comes from COMTRADE Trademap.

Table 5-5. Egypt's Top Exports in HS Chapters 84, 85, and 87, by HS 4, 2014 (US\$ 000)

| HS 4 Code | Product label | Exports to the World | U.S. Imports from Egypt | U.S. Imports from Egypt QIZ | QIZ Imports as % of All U.S. Imports from Egypt | Maximum U.S. Applied Tariff |
|-----------|---|----------------------|-------------------------|-----------------------------|---|-----------------------------|
| '8544 | Insulated wire/cable | 1,001,830 | 1,676 | 493 | 29 | 5.3% |
| '8528 | Television receivers (including video monitors & video projectors) | 749,404 | 286 | - | 0 | 5.0% |
| '8418 | Refrigerator, freezer, etc. | 122,613 | - | - | N/A | 1.8% |
| '8516 | Electric instantaneous water heater, space heating; hair dryer | 93,568 | - | - | N/A | 5.3% |
| '8537 | Board & panels, equipped with two/more switches, fuses | 37,154 | 4 | - | 0 | 2.7% |
| '8415 | Air conditioning machines, with motor-driven elements | 35,067 | - | - | N/A | 2.2% |
| '8450 | Household or laundry-type washing machines | 27,426 | - | - | N/A | 2.6% |
| '8536 | Electrical app for switching (examples, fuse, switches, etc.) not exceeding 1000 volt | 25,943 | 154 | - | 0 | 2.7% |
| '8504 | Electric transformer, static converter (for example rectifiers) | 20,398 | 5 | - | 0 | 6.6% |
| '8708 | Parts & access of motor vehicles | 16,469 | 5,318 | - | 0 | 2.5% |
| '8414 | Air, vacuum pumps; hoods incorp. a fan | 15,020 | 69 | - | 0 | 4.7% |

Note: There are data discrepancies between USITC import data reported as U.S. Imports from Egypt and UN Comtrade Data reported as Exports to the U.S. The authors attempted to use a consistent data source in each table and the most reliable for the type of comparison being conducted.

Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitc.dataweb.gov. Export data to the world comes from COMTRADE Trademap.

Table 5-6. Egypt's Top Processed Food Products, by HS4, 2014 (US\$ 000)

| No. | Product code | Product label | Exports to the World | U.S. Imports from Egypt | U.S. Imports from Egypt QIZ | QIZ Imports as % of All U.S. Imports from Egypt | Maximum U.S. Applied Tariff |
|-----|--------------|---|----------------------|-------------------------|-----------------------------|---|-----------------------------|
| 1 | '0406 | Cheese and curd | 378,924 | 2,372 | - | 0 | 25 |
| 2 | '0713 | Dried vegetables, shelled | 286,232 | 219 | - | 0 | 1.5 cents/kg |
| 3 | '1806 | Chocolate and other food preparations containing cocoa | 148,373 | 132 | - | 0 | 10 + 52.8 cents/kg |
| 4 | '0710 | Frozen vegetables | 144,671 | 10,508 | 4,792 | 46 | 14.90 |
| 5 | '2009 | Fruit & vegetable juices, unfermented | 128,334 | 7,532 | 408 | 5 | 7.9 cents/liter |
| 6 | '2005 | Prepared or preserved vegetables nes (excluding frozen) | 99,632 | 7,763 | 4,993 | 64 | 14.90 |
| 7 | '2106 | Food preparations, nes | 78,288 | 1,050 | - | 0 | 10 + 70.4 cents/kg |
| 8 | '1704 | Sugar confectionery (including white choc), not containing cocoa | 75,999 | 84 | 13 | 15 | 12.20 |
| 9 | '1703 | Molasses resulting from the extraction or refining of sugar | 56,513 | 14 | - | 0 | .35cents/kg |
| 10 | '1905 | Bread, biscuits, wafers, cakes and pastries | 55,296 | 396 | - | 0 | 4.50 |
| 11 | '2004 | Prepared or preserved vegetables nes (incl. frozen) | 53,598 | 569 | 477 | 84 | 11.20 |
| 12 | '1902 | Pasta & couscous | 53,541 | 949 | 102 | 11 | 6.40 |
| 13 | '2007 | Jams, fruit jellies & marmalades | 51,819 | 2,137 | 46 | 2 | 14 |
| 14 | '0811 | Frozen fruits & nuts | 50,584 | 1,774 | 1,749 | 99 | 14.50 |
| 15 | '1515 | Fixed vegetable fats & oils & their fractions | 46,655 | 46 | - | 0 | 3.40 |
| 16 | '0711 | Vegetables, provisionally preserved (unfit for immediate consumption) | 44,750 | 20 | 20 | 100 | 8 +8.6cents/kg |
| 17 | '0712 | Dried vegetables | 44,422 | 7,373 | 670 | 9 | 29.80 |

Note: There are data discrepancies between USITC import data reported as U.S. Imports from Egypt and UN Comtrade Data reported as Exports to the U.S. The authors attempted to use a consistent data source in each table and the most reliable for the type of comparison being conducted.

Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitc.dataweb.gov. Export data to the world comes from COMTRADE Trademap.

Table 5-7. Customs and Cost, Insurance, Freight Values for Selected Processed Foods Products at the HS 4 Level, 2014 (US \$)

| HS 4 Product Code | Product Description | All US Imports from Egypt Customs Value (CV) | All US Imports from Egypt CIF Value (CIFV) | Calculated insurance cost (CIFV-CV) | Insurance and Freight as % of Customs Value | Total U.S. Imports (CV) | Imports from Egypt as a % of all U.S. Imports |
|-------------------|--|--|--|-------------------------------------|---|-------------------------|---|
| '0406 | Cheese and curd | 2,371,856 | 2,521,648 | 149,792 | 6% | 1,274,727,560 | 0.186% |
| '0710 | Frozen vegetables | 10,508,495 | 11,341,901 | 833,406 | 8% | 833,104,346 | 1.261% |
| '2009 | Fruit & vegetable juices, unfermented | 7,531,680 | 8,502,666 | 970,986 | 13% | 1,890,483,216 | 0.398% |
| '2005 | Prepared or preserved veg. nes (excl frozen) | 7,763,266 | 8,428,981 | 665,715 | 9% | 1,132,647,954 | 0.685% |
| '2106 | Food preparations, nes | 1,050,086 | 1,090,215 | 40,129 | 4% | 2,026,126,984 | 0.052% |
| '2007 | Jams, fruit jellies & marmalades | 2,137,018 | 2,481,728 | 344,710 | 16% | 235,062,770 | 0.909% |
| '0811 | Frozen fruits & nuts | 1,773,544 | 1,845,770 | 72,226 | 4% | 733,880,443 | 0.242% |
| '0712 | Dried vegetables | 7,372,844 | 7,887,361 | 514,517 | 7% | 237,732,403 | 3.101% |

Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitc.dataweb.gov.

Table 5-8. Customs and Cost, Insurance, Freight Values for Selected Footwear Products at the HS 4 Level, 2014 (US\$)

| HS 4 Product Code | Product Description | All US Imports from Egypt Customs Value (CV) | All US Imports from Egypt CIF Value (CIFV) | Calculated insurance cost (CIFV-CV) | Insurance and Freight as % of Customs Value | Total U.S. Imports (CV) | Imports from Egypt as a % of all U.S. Imports |
|-------------------|----------------------------|--|--|-------------------------------------|---|-------------------------|---|
| '6403 | Footwear, upper of leather | \$374,843 | \$395,109 | \$20,266 | 5% | \$12,699,683,714 | 0.003% |

Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitc.dataweb.gov.

Table 5-9. Customs and Cost, Insurance, Freight Values for Selected Leather Accessories Products at the HS 4 Level, 2014 (US \$)

| HS 4 Product Code | Product Description | All US Imports from Egypt Customs Value (CV) | All US Imports from Egypt CIF Value (CIFV) | Calculated insurance cost (CIFV-CV) | Insurance and Freight as % of Customs Value | Total U.S. Imports (CV) | Imports from Egypt as a % of all U.S. Imports |
|-------------------|---|--|--|-------------------------------------|---|-------------------------|---|
| '4205 | Articles of leather or composition leather, nes | 10,662 | 12,557 | 1,895 | 18% | 207,213,363 | 0.005% |
| '4202 | Trunks, suit-cases, camera cases, handbags etc. of leather, plastic, textile etc. | 15,901 | 18,263 | 2,362 | 15% | 10,894,006,593 | 0.0001% |
| '4203 | Articles of apparel & clothing accessories, of leather or composition leather | 5,437 | 6,067 | 630 | 12% | 1,688,799,784 | 0.000% |

Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitic.dataweb.gov.

Table 5-10. Customs and Cost, Insurance, Freight Values for Selected Light Manufacturing Products at the HS 4 Level, 2014 (US \$)

| HS 4 Product Code | Product Description | All US Imports from Egypt Customs Value (CV) | All US Imports from Egypt CIF Value (CIFV) | Calculated insurance cost (CIFV-CV) | Insurance and Freight as % of Customs Value | Total U.S. Imports (CV) | Imports from Egypt as a % of all U.S. Imports |
|-------------------|---|--|--|-------------------------------------|---|-------------------------|---|
| '8544 | Insulated wire/cable | 1,122,187 | 1,175,192 | 53,005 | 5% | 18,393,410,535 | 0.006% |
| '8528 | Television receivers (including video monitors & video projectors) | 286,383 | 294,321 | 7,938 | 3% | 26,885,146,527 | 0.001% |
| '8536 | Electrical app for switching (ex: fuse, switches, etc.) not exceeding 1000 volt | 160,044 | 168,580 | 8,536 | 5% | 9,746,339,585 | 0.002% |
| '8708 | Parts & accessories of motor vehicles | 5,317,859 | 5,441,531 | 123,672 | 2% | 57,939,803,531 | 0.009% |

Source: Tariff and trade data is from the U.S. Department of Commerce and the U.S. International Trade Commission via usitic.dataweb.gov.

6. CONCLUSIONS

Of the four categories of exports considered in this study, the most promising candidate for benefitting from QIZ status is “Processed Foods”. Although obstacles are considerable, some firms have already managed to market millions of dollars of processed foods to the United States. Egyptian growers and food processors are already looking to U.S. markets for any product they cannot sell fresh locally or to EU markets at better margins. QIZ benefits would be an incentive to make the investments needed to comply with USDA and FDA standards and customs requirements for “substantial transformation”.

The fact that processed foods have been growing in absolute terms and as a share of all QIZ exports suggests that this is a product category with some intrinsic attraction to entrepreneurs and investors in Egypt and Israel as well as to importers/buyers/distributors in the United States. While the other categories seem attractive it should be instructive that even after ten years of existence or operation, no investors or entrepreneurs have judged it worthwhile to export footwear, leather accessories or electrical appliances through QIZ. This includes international operators, who, it is known, keep analysts and advisors who track U.S. trade agreement requirements and benefits and advise on sourcing and investment decisions based on overall supply chain considerations, not just tariff benefits.

Finally, every success in the case of a food product grown in Egypt will have greater economic impact on poverty reduction in Egypt than exports of products for which Egypt would have to import a substantial portion of the inputs.

When examined closely there are a number of logical reasons why exports from Egypt’s QIZ’s have been dominated by clothing and textile articles. First, Egypt was already producing and exporting RMGs to the U.S. Investment in production and access to market was already in place and functioning under the quota system that pre-dated the QIZ and the established reliable market access supported additional investment. Second, U.S. import practices are generally liberal and tariffs low except in a few categories that include clothing, footwear, dairy and foodstuffs. The tariff advantage of the QIZ therefore tends not to support a broad diversity of exports.

For future research on this topic, we recommend a closer look at the experience of Jordan and Morocco and at what industries and exports have grown to date based on the specific competitiveness constraints and tariff schedule applicable over time. Additional research using regression at the 2 and 4 digit HS code could explain how QIZ and FTA implementation in Egypt, Jordan, and Morocco impacted export growth over time.

Specific studies for specific products can be done, but these will be more useful if they can be done with provisions to consult with U.S. buyers regarding their interest in considering sourcing from Egypt for a product that has QIZ advantages.

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APPENDIX A. BACKGROUND ON THE U.S. QIZ PROGRAM AND EGYPT QIZS

Qualifying Industrial Zones (QIZ) is a U.S. trade preference program established by the U.S. Congress through legislation in 1998. It represents an important element in U.S. efforts to increase trade with Egypt by improving the competitiveness of Egyptian products through duty free privileges accorded to goods that contain a specified level of Israeli content and meet other conditions. Egypt and Israel signed an agreement in 2004 to undertake QIZs. The U.S. government designated the first QIZs in Egypt in 2004 and Egyptian firms began exporting QIZ qualifying products in 2005. The conditions for QIZ eligibility comprise three key requirements:

- Manufacture in an eligible factory located in a QIZ,
- A minimum of 35 percent of the value must originate in Egypt
- The article must incorporate at least 10.5 percent by value of Israel input¹⁵

The QIZ protocol was not intended to benefit any particular industry. However, at the time of its implementation in Egypt the Multi-Fiber Arrangement quota system was ending along with its attendant distortion of international production across probable and improbable locations around the globe. Global textile and apparel trade and production began in 2005 to more fully reflect market driven cost factors with the expiration of the Agreement on Textiles and Clothing (ATC). These changes led to the U.S. market becoming more open and competitive. Implementation of the QIZ program by Egypt in 2005 was therefore an important factor in helping Egypt's RMG sector maintain and build its exports to the increasingly competitive U.S. market.

Several factors contributed to QIZs benefiting the Egypt RMG sector. The U.S. duty rates on wearing apparel are higher than those on virtually any other product category. Moreover, Egypt had an established RMG industry with existing relationships with U.S. buyers, as well as textiles to supply Egyptian garment makers. The inputs needed to produce apparel included a variety of items that could be sourced in Israel such as textiles, chemicals, and packing materials. China, the largest global producer and super competitor in the garment industry, remained under a system of quantitative restraints until 2008, a constraint that afforded Egypt

¹⁵ Definitions of terms such as "originating" and the process for valuation are those of customs authorities, which may occasionally vary from common understanding, but are not so arcane that a company with sound accounting practices and good general understanding cannot verify the eligibility of its products.

an opportunity to solidify and expand its share of the U.S. market in large measure through the QIZ program.

Between 2005 and 2008, QIZ exports (mostly apparel) more than tripled from \$266 million to \$874 million. After 2008 QIZ exports grew more slowly, to approximately US\$1 billion in 2011.

APPENDIX B. SCOPE OF WORK

Statement of Work

TFP-150513-01

CONTRACT NO. AID-263-C-11-00003

Updated Report on QIZ Program Diversification into new Export Sectors

| | |
|-------------------------|---|
| Positions: | Trade Analysts |
| SOW Task: | Updated Report on QIZ Program Diversification |
| Dates: | On or about April 20 to July 31, 2015. |
| Staff & LOE: | Mr. John Varley, 7 days LOE Ms. Jeannette Paulino, 10 days LOE Ms. Leanne Sedowski, 8 days LOE Mr. Stewart Pierce-Gardner, 13 days LOE |

BACKGROUND—GENERAL

The USAID-funded Egypt Trade Facilitation Project (TFP) [AID -263-C-11-0003] contributes to USAID/Egypt's assistance objective, working to improve conditions for trade and investment, and support the overall USG strategic economic partnership with Egypt signed in May 2009. The ultimate objective of this four-year project is to promote economic growth and job creation, reducing poverty through improvements in the trade environment. More specifically, Egypt TFP focuses on reducing barriers to trade and the creation of a more efficient internal and external trading system that streamlines the flow of goods at the border and leads to improved administration and growth in Egypt's trade of goods and services within its border. The results of this project are categorized in two groups: Results 1: reform measures that take place at the border and Result 2: those reforms that occur behind the border.

Enabling Egypt to export more competitively is part of the overall objective the Trade Facilitation Project (TFP). There is no Free Trade Agreement between Egypt and the United States. Qualified Industrial Zones (QIZs) are part of the overall strategy to assist economic development in Egypt by helping to improve Egypt's competitiveness in trade with the U.S. Because it utilizes certain provisions of the U.S.-Israel Free Trade Agreement (FTA), the QIZ protocol is actually a tri-nation agreement. With the signing of the Egypt-Israel QIZ Protocol, in December 2004, the United States agreed to grant duty- and quota-free market access to imports manufactured by companies located within designated areas or "Qualified Industrial Zones (QIZs)" in Egypt, provided that those products comply with the protocol-stipulated rules of origin. Specifically, Article II/D/1.a of the Egypt-Israel QIZ protocol, which addresses the rules of origin, requires that 35 percent of a product's value must be added through manufacturing in Egypt, in accordance with U.S. requirements for QIZs, and at least 10.5 percent of the value must originate in Israel.

Because it came into existence just as the quota system governed by the Multi-Fiber Agreement expired (December 2004), the QIZ Protocol provided timely opportunities to companies in Egypt's RMG and textiles sector. Exports in these two categories rose quickly to more than \$1 billion by 2010, firmly establishing the program as a policy success. However, few industries outside the RMG/textile sector have managed to take similar advantage of QIZ opportunities. RMG and textiles account for well over 90 percent of all QIZ exports. While total QIZ exports rebounded in 2014 from their drop in 2013 by about 2 percent, the share of exports other than RMG/textile products dropped by over 11 percent from 2013 to 2014.

Lack of diversification limits the potential growth of the QIZ program. Expanding the program could result in increased job creation, closer trade ties between Egypt and the United States, and increased commercial ties between Egypt and Israel.

The QIZ's main benefit to exporters is its exemption from quotas and tariffs, and because the U.S. tariff structure for most products is zero or very low, such products would not benefit from QIZ status. There are products, however, where U.S. tariffs remain significant and for these, the exemption conferred by QIZ status could be significant, if the products can be produced competitively within the designated zones in Egypt. Identifying such product category export opportunities could help increase Egyptian exports to the United States and support Egyptian goals for increased employment.

OBJECTIVE

The objective of this assignment is to update the sections of the report TFP produced in February 2013, "QIZ Study: Findings, Conclusions and Recommendations," that discussed initial prospects for diversification by the QIZ Program into new export sectors. TFP has been requested to produce an update to these sections by USAID/Egypt, at the suggestion of members of the Economic Working Group at the U.S. Embassy/Cairo.

The purpose of producing an updated report is to update the data related to the three additional product sectors identified in the previous report that might benefit from the QIZ program. The 2013 TFP study identified three sectors worthy of additional study: footwear, leather accessories and processed foods. This report will examine the prospects for these sectors in greater detail and examine general prospects for selected products in an additional sector—light manufacturing.

DESCRIPTION OF ACTIVITY

This activity will analyze prospects for diversification by the QIZ Program into four export sectors. It will update and build on the analysis of diversification prospects provided in TFP's "QIZ Study: Findings, Conclusions and Recommendations," produced in February 2013.

The methodology will utilize measures of export potential such as Egypt's share of world markets, share of product and market in total exports, trade intensity and export diversification indices, revealed comparative advantage, and others, to measure the kinds of products and new markets in which Egypt has trade potential. It will also provide examples of products in the four potential export sectors indicated below that are eligible for the greatest tariff advantages under the QIZ Program.

Assessing export competitiveness prospects will include the following tasks:

1. Assess the Processed Foods Sector—Analyze prospects to diversify beyond traditional products such as processed olives, olive oil, and other products that target ethnic markets; assess new products' ability to comply with specific locational requirements for QIZ eligibility, and related traceability requirements, and other competitiveness factors.
2. Assess the Footwear Sector—Assess competitiveness prospects and sector constraints, e.g., limited entrepreneurial experience, current focus on traditional management techniques among manufacturers, and related competitiveness factors.
3. Assess Leather Accessories—Assess competitiveness prospects, e.g., limited cost competitiveness, high transport costs, lack of proximity to major raw material suppliers, environmental/water constraints and other key competitiveness factors.
4. Assess Light Manufacturing—Assess general competitiveness prospects and sector constraints for selected light manufacturing products.
5. Update product categories offering the greatest “tariff benefit” to Egypt that have relatively high U.S. tariffs within the above four sectors. Identify the top products in each sector by HTS chapter subject to the highest tariffs but eligible for the QIZ program.
6. Provide market information on products identified in item 5 as offering the greatest tariff benefit, including current suppliers, their respective market shares in the U.S. market, and average CIF prices in the United States. Provide estimates of FOB prices of these products at a reference port in Egypt and compare these estimates to equivalent wholesale prices in Egypt in the same reference port.
7. Use appropriate measures of export potential and other analytical methodologies, including summary reviews and comparisons of export product categories that have increased under similar QIZ and FTA preferential tariff programs in regional comparator countries such as Jordan and Morocco in recent years.

DELIVERABLES

The consultants will report to TFP Chief of Party Lindsey Wellons, who will approve all deliverables.

1. A report updating prospects for QIZ Program diversification into new export sectors, including chapters or sections on each of the tasks above, with annexes on the most recent export statistics related to the QIZ Program.
2. Presentations, if necessary, summarizing the report to USAID/Egypt and or to economic officials at U.S. Embassy Cairo.
3. Related items as necessary.

TIMEFRAME AND PROPOSED LOE

The timeframe for this assignment will be from on or about April 20 to July 31, 2015. It is proposed that consultant Stewart Pierce-Gardner travel from Washington to Cairo, o/a May 16 to o/a May 22, for about 7 days LOE including travel time, to collect data and conduct interviews.

Total estimated LOE will be, for:

- John Varley, 7 person-days LOE (no travel). Tasks and LOE:

- Conduct literature review and background research (2 days)
- Select most appropriate methodologies for measuring export potential for each sector and analyze similar QIZ and FTA preferential tariff programs in regional comparator countries (3 days);
- Review final report and annexes. (2 days)
- Jeannette Paulino, 10 person-days LOE (no travel). Tasks and LOE:
 - Contribute to analysis of export potential focusing on food products (3 days)
 - Conduct HS code research to identify the top products in each sector by chapter that incur the highest tariffs but are eligible for U.S. preferential tariff exemption under QIZ (4 days)
 - Draft narrative for the above sections and review final report and annexes (3 days).
- Leanne Sedowski, 8 person days LOE, including 2 preparation days and 3 days drafting report sections. Tasks and LOE:
 - Preparation before travel—review background, set appointments (2 days)
 - Draft report sections (6 days)
- Stewart Pierce-Gardner, 13 person days LOE, including 3 days for RT travel Washington-Cairo, 5 days' work in Cairo, and 5 days for drafting, finalizing report, and presenting final report if necessary (during close-out in late July).
 - Meetings / data collection in Cairo (5 days)
 - Draft report sections, supervise & finalize other consultant contributions, present draft report if necessary (5 days)
 - Travel RT (3 days)

ACTIVITY CONSULTANTS

The international consultants/advisors recommended for this assignment include:

Mr. John Varley, a senior trade specialist and long-term Nathan Associates employee who served previously as Chief of Party of TFP from June 2011 to June 2014, and contributed to and oversaw the previous TFP QIZ Reports done in 2012 and 2013.

Ms. Jeannette Paulino, research associate, who has been project manager of Egypt TFP for over three years. She has previously worked on QIZ-related research by collecting and analyzing trade data for the potential expansion of the QIZ program in Upper Egypt and the potential effect on the United States garment industry. She has also prepared statistical tables on Egyptian exports to the United States and Egyptian imported-products recalled by the United States for the Egyptian Organization for Standardization and Quality (EOS).

Ms. Leanne Sedowski, Managing Associate, Trade Policy, International Development Economics at Nathan Associates, who contributed to the TFP QIZ Reports in 2012 and 2013.

Mr. Stewart Pierce-Gardner, Associate, Trade Facilitation, International Development Economics at Nathan Associates, who has been project manager of Egypt TFP for over 3 years.

COUNTERPARTS

This report will be prepared for USAID/Egypt. No counterpart from the QIZ Unit is designated.

OTHER TFP RESOURCES

TFP personnel including management and expert consultants will be available to assist the consultants on this task.

APPENDIX C. TRADE DATA ANALYSIS

As part of this assessment and report TFP undertook trade analysis in May and June 2015 to identify sectors other than RMG offering the potential to diversify and increase QIZ exports.¹⁶ All data are from www.trademap.org of the International Trade Centre and are based on UN COMTRADE statistics. Data was analyzed down to the Harmonized System (HS) 6-digit level.

Selection of the products listed below was guided by the following criteria:

- The only products included are those with U.S. tariff lines of 10 percent or higher, a rate range consistently identified by QIZ firms as necessary to make QIZ exports price competitive.
- QIZ exports were excluded, as these products have already been identified as areas of potential.
- Apart from leather goods and footwear, the focus was on Egyptian products with exports values greater than \$1 million as this amount suggests that a sector is of sufficient scale and competitiveness to enable expansion into the U.S. market is possible.

Overall, the data show that Egypt exports significant amounts of high-tariff processed or semi-processed agricultural products to the world. Specifically, Egyptian firms have succeeded in exporting significant amounts of agricultural and food products to the European Union, which has strict sanitary and phytosanitary requirements. Exports of leather and footwear products were also analyzed. However, out of the 26 footwear and leather tariff lines with a tariff of 10 percent or above, Egypt does not export footwear products in amounts greater than \$1 million.

Egypt exports 96 products (at the HS6 level) in excess of \$1 million to the world that have a U.S. tariff greater than 10 percent but are not currently exported to the U.S. under the QIZ program. The top 25 products in Table C-1 represent 84 percent of these exports. Of these 25, agricultural exports make up 47 percent of the top 25, while fiber products (yarns, fabrics, napkins) are the next largest grouping (16 percent).

¹⁶ This research built upon trade data analysis conducted for the July 2012 USAID-funded report prepared by Nathan Associates, *Impact of Proposed Expansion of Qualifying Industrial Zones in Egypt*.

Table C-1. Egypt's Top 25 Exports to the World of Greater than \$1 million with a U.S. Tariff of 10% or Higher, 2014

| HS Subheading | HS Subheading description | Value in 2014 US\$ thousand |
|---------------|---|-----------------------------|
| 040630 | Cheese processed, not grated or powdered | 236,894 |
| 961900 | Sanitary towels (pads) and tampons, napkins and napkin liners for babies, & similar article | 164,345 |
| 690810 | Tiles, cubes and sim <7 cm rect or not etc, glazed ceramics | 149,469 |
| 040610 | Cheese, fresh (including whey cheese) unfermented, and curd | 102,749 |
| 701391 | Glassware nes of lead crystal (other than that of 70.10 or 70.18) | 83,426 |
| 210690 | Food preparations nes | 72,476 |
| 690710 | Tiles, cubes and sim <7 cm rect or not etc, unglazed ceramics | 67,196 |
| 150710 | Soya-bean oil crude, whether or not degummed | 48,240 |
| 080410 | Dates, fresh or dried | 47,319 |
| 200799 | Jams, fruit jellies ,fruit/nut purée & paste, ckd prep, sugared, sweetend/not | 42,208 |
| 170490 | Sugar confectionery nes (including white chocolate), not containing cocoa | 40,764 |
| 150790 | Soya-bean oil and its fractions, refined but not chemically modified | 39,719 |
| 210320 | Tomato ketchup and other tomato sauces | 32,094 |
| 040690 | Cheese nes | 31,857 |
| 701310 | Glassware of a kind used for table kitchen, etc. of glass-ceramics | 30,480 |
| 120242 | Groundnuts, shelled, whether or not broken (excl. seed for sowing, roasted or otherwise co | 27,492 |
| 520819 | Woven fabrics of cotton,>=85%, not more than 200 g/m2,unbleached, nes | 27,218 |
| 540710 | Woven fab of high tenacity fi yarns of nylon other polyamides/polyesters | 17,788 |
| 200899 | Fruits & oth edible pts of plants nes, prep/presvd, sug, sweet/spir/not | 16,052 |
| 550810 | Sewing thread of synthetic staple fibres | 14,225 |
| 701337 | Drinking glasses (excl. glasses of glass ceramics or of lead crystal a | 13,425 |
| 520859 | Woven fabrics of cotton,>=85%, not more than 200 g/m2,printed, nes | 12,549 |
| 630499 | Furnishing articles nes, of other textile materials, not knitted or crocheted | 10,557 |
| 080711 | Watermelons, fresh | 10,237 |
| 630800 | Sets consisting of woven fab & yarn, for making up into rugs, tapestries etc. | 9,809 |

Agricultural products were also identified as a potential area of expansion for QIZ firms and further research was done. Table C-2 illustrates all the processed or semi-processed agricultural products with tariffs at 10 percent or above that are exported from Egypt to the world in excess of \$1 million. None of these product lines is exported from Egypt to the United States under the QIZ regime in significant quantities.

Table C-2. Egypt's Agricultural and Food Product Exports to the World in 2014 Greater than \$1 million and with a U.S. Tariff of 10% or Greater

| HS Subheading | HS Subheading description | Value in 2014 (US\$ thousand) |
|---------------|--|-------------------------------|
| 040630 | Cheese processed, not grated or powdered | 236,894 |
| 040610 | Cheese, fresh (including whey cheese) unfermented, and curd | 102,749 |
| 150710 | Soya-bean oil crude, whether or not degummed | 48,240 |
| 080410 | Dates, fresh or dried | 47,319 |
| 170490 | Sugar confectionery nes (including white chocolate),not containing cocoa | 40,764 |
| 150790 | Soya-bean oil and its fractions, refined but not chemically modified | 39,719 |
| 040690 | Cheese nes | 31,857 |
| 120242 | Groundnuts, shelled, whether or not broken (excl. seed for sowing, roasted or otherwise co | 27,492 |
| 080711 | Watermelons, fresh | 10,237 |
| 071010 | Potatoes, frozen | 9,795 |
| 040229 | Milk and cream powder sweetened exceeding 1.5% fat | 8,544 |
| 200290 | Tomatoes nes, prepared or preserved other than by vinegar or acetic acid | 8,079 |
| 040620 | Cheese, grated or powdered, of all kinds | 7,377 |
| 040590 | Fats and oils derived from milk nes | 2,935 |
| 080719 | Melons, fresh, other than watermelons | 2,831 |
| 151790 | Edible mx/prep of animal/veg fats & oils/of fractions ex hd No 15.16 | 2,661 |
| 100630 | Rice, semi-milled or wholly milled, whether or not polished or glazed | 2,410 |
| 190420 | Prepared foods of unroasted cereal flakes, mixtures | 2,125 |
| 190490 | Cereals, exc maize (corn),in grain form, pre-cookd or otherwise preparad | 1,848 |
| 070610 | Carrots and turnips, fresh or chilled | 1,839 |
| 190110 | Prep of cereals, flour, starch/milk f infant use, put up f retail sale | 1,749 |
| 081350 | Mixtures of edible nuts or dried fruits of this chapter | 1,299 |
| 190190 | Malt extract & food prep of Ch 19 <50% cocoa&hd 0401 to 0404 < 10% cocoa | 1,248 |
| 200110 | Cucumbers and gherkins, prepared or preserved by vinegar or acetic acid | 1,182 |
| 070420 | Brussels sprouts, fresh or chilled | 1,136 |

As mentioned in the main body of the report, leather and footwear products are areas of potential expansion for QIZ firms as Egypt has a potential comparative advantage in these sectors. Table C-3 lists the HS6-level product lines of general leather goods and footwear products with tariffs of 10 percent or more that are exported from Egypt to the world. None of these product lines is exported from Egypt to the United States under the QIZ regime.

Table C-3. Egypt's Leather and Footwear Exports to the World in 2014, with Tariff Lines of 10% or Higher not Exported under QIZ to the U.S. Market

| | HS Subheading | HS Subheading description | Value in 2014 (US\$ thousand) |
|-------------------|----------------------|---|--------------------------------------|
| Leather Goods | 420212 | Trunks, suit-cases & sim container w/outer surface of plastics/textiles | 57 |
| | 420219 | Trunks, suit-cases and similar containers, nes | 15 |
| | 420222 | Handbags w outer surface of sheeting of plastics o of textile materials | 4 |
| | 420299 | Containers, nes | 1 |
| | 420329 | Gloves mittens & mitts, o/t for sport ,of leather or of composition leather | 0 |
| | 420229 | Handbags, of vulcanised fibre or of paperboard | 0 |
| | 420232 | Articles carried in pocket/handbag, w/outer surface sheetg of plas/tex | 0 |
| | 420239 | Articles carried in pocket or handbag, nes | 0 |
| Footwear Products | 640590 | Footwear, nes | 387 |
| | 640299 | Footwear, outer soles/uppers of rubber or plastics, nes | 229 |
| | 640291 | Footwear, outer soles/uppers of rubber or plastics, coverg the ankle, nes | 212 |
| | 640359 | Footwear, outer soles and uppers of leather, nes | 186 |
| | 640690 | Parts of footwear; removable in-soles, heel cushions and similar articles; gaiters, legging | 109 |
| | 640610 | Uppers and parts thereof, other than stiffeners | 108 |
| | 640419 | Footwear o/t sports, w outer soles of rubber/plastics & uppers of tex mat | 100 |
| | 640199 | Waterproof footwear, outer soles/uppers of rubber or plastics, nes | 68 |
| | 640351 | Footwear, outer soles and uppers of leather, covering the ankle, nes | 57 |
| | 640420 | Footwear with outer soles of leather and uppers of textile materials | 22 |
| | 640219 | Sports footwear, outer soles and uppers of rubber or plastics, nes | 21 |
| | 640520 | Footwear with uppers of textile materials, nes | 11 |
| | 640192 | Waterproof footwear, outr sole/upper of rbr/plas, covg ankle nt knee nes | 8 |
| | 640319 | Sports footwear, o/t ski, outr sole of rbr/plas/leather & upper of leather | 5 |
| | 640510 | Footwear with uppers of leather or composition leather, nes | 2 |
| | 640411 | Sports footwear w outer soles of rubber o plastics& uppers of tex mat | 0 |

For the final the analysis, Egypt's exports in 2014 to the European Union were examined. As with other analyses, the focus was on products with a U.S. tariff line of 10 percent or above, and all exports above \$1 million. Of particular interest are the agricultural products, because the European Union's agricultural export requirements are much stricter than those of the United States. An agricultural product exported to the European Union could potentially meet U.S. sanitary or phytosanitary requirements, although further research is required to determine the size of the market in the United States.

Table C-4. Egypt's Exports to the European Union in 2014, greater than \$1 million and with a U.S. tariff of 10 percent or higher

| HS Subheading | HS Subheading description | Value in 2014 (US\$ thousand) |
|----------------------|---|--------------------------------------|
| 520819 | Woven fabrics of cotton,>/=85%, not more than 200 g/m2,unbleached, nes | 25,656 |
| 200899 | Fruits & other edible pts of plants nes, prep/presvd, sug, sweet/spir/not | 11,341 |
| 520859 | Woven fabrics of cotton,>/=85%, not more than 200 g/m2,printed, nes | 10,603 |
| 630499 | Furnishing articles nes, of other textile materials ,not knitted or crocheted | 7,460 |
| 520811 | Plain weave cotton fabric,>/=85%, not more than 100 g/m2, unbleached | 6,368 |
| 630800 | Sets consisting of woven fab & yarn, for making up into rugs ,tapestries etc. | 6,113 |
| 701391 | Glassware nes of lead crystal (other than that of 70.10 or 70.18) | 5,221 |
| 610331 | Mens/boys jackets and blazers, of wool or fine animal hair, knitted | 4,921 |
| 620291 | Womens/girls anoraks & similar article of wool/fine animal hair, not knit | 4,464 |
| 691110 | Tableware and kitchenware of porcelain or china | 4,418 |
| 210320 | Tomato ketchup and other tomato sauces | 3,796 |
| 540831 | Woven fabrics of artificial filaments, unbleached or bleached, nes | 3,600 |
| 630319 | Curtains, drapes, interior blinds & curtain/bd valances, oth tex mat, knit | 2,990 |
| 200510 | Homogenized vegetables prep/presvd , o/t by vinegar/acetic acid, not frozen | 2,963 |
| 200290 | Tomatoes nes, prepared or preserved oth than by vinegar or acetic acid | 2,811 |
| 200880 | Strawberries nes,o/w prep/presvd, whether/not sugard, sweet/spiritd | 2,560 |
| 210690 | Food preparations nes | 2,167 |
| 701328 | Drinking glasses, stemware (excl. of glass ceramics or of lead crystal | 1,995 |
| 690810 | Tiles, cubes and sim <7 cm rect or not etc, glazed ceramics | 1,825 |
| 551519 | Woven fabrics of polyester staple fibres, nes | 1,686 |
| 611599 | Hosiery nes, of other textile materials, knitted | 1,525 |
| 520822 | Plain weave cotton fabric,>/=85%, >100 g/m2 to 200 g/m2, bleached | 1,511 |
| 511119 | Woven fabrics of carded wool/fine animal hair,>/=85% by wght,>300 g/m2 | 1,393 |
| 701337 | Drinking glasses (excl. glasses of glass ceramics or of lead crystal a | 1,377 |
| 620590 | Mens/boys shirts, of other textile materials, not knitted | 1,347 |
| 441510 | Cases, boxes, crates, drums & similar packings; cable-drums, wooden | 1,338 |

ANNEX D. TEXT OF QIZ PROTOCOL

PROTOCOL BETWEEN THE GOVERNMENT OF THE ARAB REPUBLIC OF EGYPT AND THE GOVERNMENT OF THE STATE OF ISRAEL ON QUALIFYING INDUSTRIAL ZONES

The Government of the Arab Republic of Egypt and the Government of the State of Israel (hereinafter “the Parties”) noting the 25th Anniversary of the signing of the Peace Agreement between the Parties and desiring to promote economic and trade relations for the benefit of the Parties have agreed to conclude this protocol.

In recognition of the requirements in Section 9 of the United States-Israel Free Trade Area Implementation Act of 1985, as amended, and Proclamation No. 6955 of the President of the United States of America, hereinafter “the legislation and proclamation” and on the recommendation of the private sector of the Parties have agreed to the creation of the Qualifying Industrial Zones (hereinafter the “QIZ”), and request the Government of the United States to designate them as “Qualifying Industrial Zones” under the legislation and proclamation.

ARTICLE I GEOGRAPHIC BOUNDARIES

The Parties hereby designate the following territories of their respective countries as enclaves where merchandise may enter for purposes of export, without payment of duty or excise taxes, no matter what the country of origin of the merchandise.

A. For the Government of Egypt: areas as designated by the Parties and as approved by the United States Trade Representative (USTR) and as specified in Annex A to this protocol.

B. For the Government of Israel: An Area under Israeli Customs control within the boundaries of the land crossing border at Nitzana Crossing Point.

On the basis of the respective national legislation of the Parties, the competent authorities of Israel and Egypt shall establish the necessary procedures for the purpose of assuring the speedy flow of goods into and out of these areas. The purpose of these procedures is to ensure the strict enforcement of the principles of duty and taxation pursuant to this protocol.

In the case of the State of Israel, where factories located outside the zone shall contribute part of the 35 percent minimum content required by the legislation and proclamation, the Israeli

customs authority shall ensure that inputs imported from abroad incorporated into goods shipped into the zone shall be exempt from duty.

ARTICLE II

QIZ JOINT COMMITTEE

A. The Parties hereby agree to the establishment of a QIZ Joint Committee which shall have the responsibilities, outlined in Annex B, of identifying those manufacturers located within the Qualifying Industrial Zones, which involve substantial economic cooperation between Israel and Egypt. Goods processed in these zones by manufacturers whose names appear on a list (hereinafter “the list”) approved by the QIZ Joint Committee shall be eligible for duty-free entry into the United States if the goods meet the requirements of this Protocol and its Annexes as well as of the legislation and proclamation.

B. The QIZ Joint Committee shall meet in Jerusalem and in Cairo, alternately, every three months or upon request by either Party whichever comes earlier. During every fourth quarter the QIZ Joint Committee shall hold a business cooperation event in which business people and other persons of both Parties who have interest in the QIZ shall have the opportunity to participate. This event shall be held in Egypt and Israel alternately.

C. A representative of the United States shall have the right to participate in meetings of the QIZ Joint Committee as an observer.

D. The QIZ Joint Committee may determine that a business qualifies for QIZ treatment if:

1.a. The company of the Egyptian side of the QIZ and the company of the Israeli side each contribute and maintain at least one third (10.5 percent) of the minimum 35 percent of local content required under the legislation and the proclamation for duty-free treatment in the United States and according to the procedures as detailed in Annex B to this Protocol; or

1.b. The manufacturer on the Egyptian side of the QIZ and the manufacturer on the Israeli side each contributes and maintains at least 20 percent of the total cost of production of goods eligible for duty-free treatment, excluding profits, even if the costs cannot be considered as part of the 35 percent minimum content requirement. For this purpose, costs may include originating materials, wages and salaries, design, research and development, depreciation of capital investment, overhead including marketing expenses, etc.

2. Only Israeli companies operating in areas under Israel’s customs’ control shall be recognized for the purposes of applying the Israeli contribution as mentioned in subsections 1.a. and 1.b. above.

E. The QIZ Joint Committee shall issue a certificate, valid for a period of one year, recognizing that a company is located within the QIZ.

1. Only companies located in areas specified in Article I may be eligible to request such a certificate.

2. This certificate will be valid for the purpose of eligibility for duty free treatment under the provisions of this Protocol, only when the company’s name appears on the list, described in Paragraph F below.

3. The QIZ Joint Committee shall have the authority to cancel this certificate only if the requirements of this Protocol and its Annexes are not met.

F. The QIZ Joint Committee shall promptly provide quarterly the U.S. Customs Authority (Trade Compliance Office, Office of Field Operations) and the Egyptian Customs Authority with a list of Companies entitled to duty free treatment for the next quarter only, according to the provisions of this Protocol.

Only companies which have fulfilled all the requirements of this Protocol and its Annexes for the previous quarter shall be eligible to be included in the list for the next quarter.

ARTICLE III RULES OF ORIGIN

The Parties agree that the origin of any textile or apparel product that is processed in the Qualifying Industrial Zones, regardless of the origin of place or processing of any of its inputs or materials prior to entry into, or subsequent to withdrawal from, these zones, shall be determined solely pursuant to the rules of origin for textile and apparel products set out in Section 334 of Uruguay Round Agreement Act, 19 U.S.C. 3592.

ARTICLE IV CUSTOMS VERIFICATION

The Parties shall assist United States authorities in obtaining information, including means of verification, for the purpose of reviewing transactions for which duty-free access into the U.S. is claimed, in order to verify compliance with applicable conditions, and to prevent unlawful transshipment of articles not qualified for duty-free access into the U.S.

ARTICLE V AMENDMENTS

Annexes to this Protocol shall be amended by the QIZ Joint Committee and upon approval by the United States.

ARTICLE VI ENTRY INTO FORCE

This Protocol shall enter into force upon the notification of both Parties on the completion of the necessary legal procedures required by them for the entry into force of this Protocol.

Done at Cairo, Egypt on December 14, 2004, in two original copies in the English language.

For the Government of the Arab Republic of Egypt For the Government of the State of Israel

Annex A. QIZ

Factories in QIZ

Industrial Cities in QIZ

Greater Cairo QIZ

Cairo Cotton

Dice

E.T.C.

Samir Flaneles

Delta

Tenth of Ramadan

Fifteenth of May (Helwan)

South of Giza

Shobra El-Khema

Nasr City

Alexandria QIZ

El-Amria (Bourg El-Arab),

Alexandria

Suez Canal Zone QIZ

Port Said Industrial City

Annex B. QIZ Joint Committee

1. A QIZ Joint Committee shall be established, in accordance with Article II of the Protocol, with two co-chairpersons: an Egyptian appointed by the Egyptian Government, and an Israeli appointed by the Israeli Government. A representative of the United States may attend the meetings as an observer

2. The responsibilities of the QIZ Joint Committee shall be to:

- Supervise the implementation of the QIZ Protocol
- Verify full compliance with the QIZ requirements
- Issue and/or cancel certificates pursuant to Article E of the Protocol;
- Determine the lists of companies pursuant to Article F of the Protocol;
- Prepare an annual report that to be submitted to the relevant Ministers

3. The QIZ Joint Committee shall carry out its responsibilities on a quarterly basis as per the following periods:

- January 1–March 31
- April 1–June 30
- July 1–September 30
- October 1–December 31

(hereinafter: “quarters”)

4. The certificate issued by the QIZ Joint Committee, pursuant to Article E of the Protocol, shall include the following information: name, address, tel. /fax numbers, e-mail address and contact person.

5. The QIZ Joint Committee shall convene quarterly, pursuant to Article II.B of the Protocol, in order to determine the list of companies, in accordance with Article F of the Protocol. The hosting Party shall issue an invitation to the other Party for a date after which both Parties have received the documents mentioned in paragraphs 6A and 6B below, but no later than 45 days after the end of the previous quarter. The meeting of the QIZ Joint Committee shall take place on a mutually agreed upon date, within 10 days from the proposed date.

6. In order for the QIZ Joint Committee to determine the lists of companies to appear on the lists pursuant to Article F of the Protocol the following procedures must be followed:

A. The company shall provide its Authorities evidence of full compliance with all the requirements of the QIZ Protocol for the previous quarter, no later than 15 days from the end of each quarter. This evidence shall include the following:

- a. Name of company, address, tel./fax numbers, e-mail addresses, contact person,
- b. Type of products exported,
- c. Type of input purchased, documented by copies of invoices from Egyptian/Israeli suppliers and list of Egyptian/Israeli suppliers in the last quarter, including contact persons,

- d. Total export of the company to the United States under the QIZ duty free treatment for the previous quarter, supported by relevant documents.

B. The authorities of the Party receiving the documents and evidence shall submit to the authorities of the other Party, no later than 30 days from the end of each quarter all quarterly data as specified in paragraph 6.A. above.

C. The QIZ Joint Committee shall verify the data specified in paragraph 6.A. in order to determine whether the requirements of the Protocol, particularly Article II.D., and the Annexes, particularly paragraphs 9, 10 and 11 of Annex B, have been fulfilled.

7. The Joint Committee shall issue the quarterly lists according to the following:

A. A company that fulfills the requirements of the Protocol and its Annexes shall appear on the list for the first two quarters following the entry into force of the Protocol.

B. For the periods that follow the first two quarters after the entry into force of the Protocol :

- i. The QIZ Joint Committee shall determine the list for the following quarter, based on the company's fulfillment of the requirements of the Protocol and its Annexes for the previous quarter.
- ii. Companies that have not previously exported under the QIZ Protocol, and that request to be included in the list determined by the QIZ Joint Committee after a quarter has already begun, will not be required to report until the end of the next full quarter.

8. If any Party fails to attend the quarterly QIZ Joint Committee meeting as required in Article II.B. of the Protocol, the Party that has attended the meeting may carry out the responsibilities of the QIZ Joint Committee. If the hosting Party fails to issue the invitation to the other Party to attend the meeting, the other Party may carry out the responsibilities of the QIZ Joint Committee.

9. The Israeli inputs that shall be recognized for the purpose of the QIZ must be direct relevant inputs.

10. The QIZ Joint Committee shall not recognize inputs purchased from Israeli enterprises as fulfilling the minimum content required from Israeli manufacturers unless those inputs fully comply with the rules of origin as stipulated in the U.S.-Israel Free Trade Area Agreement.

11. Compliance with criteria set forth in Article II.D. of the Protocol will be calculated on the basis of total duty free export to the United States under the QIZ on a quarterly basis per company and in accordance with the conditions set forth in paragraphs 9 and 10 above.

12. In the event the QIZ Joint Committee finds that a company fails to comply, for any reason, with the requirements of the QIZ Protocol and its Annexes, the following steps shall be taken:

- a. for a first-time failure - the company will not be eligible for QIZ approval for the following quarter.
- b. for a second-time failure - the company will not be eligible for QIZ approval for the following two quarters.

- c. for every failure beyond the second time - the company will not be eligible for QIZ approval for the following four quarters.

13. In case there is a need for additional data in order to verify QIZ compliance, the QIZ Joint Committee may request the U.S. Customs Authorities to provide the necessary data.

14. In case the QIZ Joint Committee finds during the implementation of the above mentioned procedures a need to amend these procedures, it will submit a proposal to the Minister of Foreign Trade and Industry of Egypt and the Minister of Industry , Trade and Labor of Israel, for their approval.

APPENDIX E. QIZ UNIT OVERVIEW

GOAL MISSION AND MANDATED TASKS

The QIZ Unit is located in the Ministry of Industry and Foreign Trade (MIFT). It is part of the Technical Office of Minister and was created to serve as an executive and technical support unit for the Egyptian side of the Joint Committee that is vested with managing the implementation process of the terms of the Protocol (see Appendix D). According to its website, the unit's goal is "to maximize the value that qualified Egyptian companies can obtain from the flow of custom-free Egyptian goods to the United States." The QIZ Unit's stated mission comprises three tasks:

QIZ MISSION STATEMENT

- Enable successful implementation of the QIZ Protocol
- Act as the implementation arm for Egypt on the Joint Committee¹⁷
- Coordinate with the other stakeholders in government and private sector

According to information on the website the Unit is mandated to carry out many tasks, the most of important of which are:

- Receiving applications from the Egyptian companies located in the QIZ designated zones and willing to be included in the List of companies entitled to the U.S. customs preferential treatment under the QIZ protocol.
- Reviewing merits of such applications in terms of their meeting all geographic and rules of origin requirements of the Protocol.
- Auditing compliance of the companies on the QIZ list in order to determine whether they still meet qualification requirements, hence remain on the List or be suspended if found noncompliant.
- Serving as an information center for local and foreign businesses interested in doing business under the terms of the QIZ protocol.
- Providing decision support services to members of the Egyptian side of the Joint Committee through compiling data and statistics on all QIZ-related activities, analyzing this information and putting forward recommendations accordingly.

All the above are primarily technical and reporting functions but the same website also lists "matchmaking" and "investment promotion" as activities within the scope of the QIZ

¹⁷ The "Joint Committee" is established by Article II of the Egypt-Israel QIZ Protocol; it is comprised of representatives of Egypt and Israel who confer on and administer QIZs in quarterly meetings.

responsibility to help make maximize the value of the QIZ protocol opportunity to qualified Egyptian businesses.

QIZ ORGANIZATION AND RESPONSIBILITIES

The QIZ Unit website describes the unit as having five departments: Administration, Communication and Information, Matchmaking, Promotion and Business Development and IT & Decision Support. Currently the unit seems to operate using a simpler model of three working groups, each comprised of four staff members that focus on its three core responsibilities:

- Registration and Joint Committee
- Audit
- Data Collection and Analysis

The following summary of the unit procedures and tasks is derived from meetings with QIZ officials, the QIZ Unit website, interviews with QIZ producers, and the TFP team's prior studies of QIZ operations.¹⁸ These tasks play an integral part in Egypt meeting its responsibilities in its joint management of QIZs with Israel and assuring that QIZ exporters meet U.S. requirements for the QIZ program. Collectively these efforts help to assure the integrity of a program on which the U.S. government places high priority.

The tasks of the unit are:

- **Registration of QIZ companies:** The Unit administers applications by firms submitted in part through an on-line application system to be designated as eligible to participate in the QIZ program. The companies must be located in a Qualifying Industrial Zone and verify that their products meet program requirements for Egyptian and Israeli content requirements. All companies must re-register annually to validate their QIZ status. As of December 2012, approximately 850 companies were registered as QIZ eligible.¹⁹
- **Quarterly Review:** The Unit conducts a quarterly review of the activities of all QIZ exporters. QIZ firms must submit to the Unit an Excel spreadsheet and supporting documentation summarizing their import of Israeli materials and their exports. The Unit reviews and verifies that all required trade procedures were followed and official stamps are genuine and legible. To be included on the joint committee approved list of QIZ firms for the upcoming quarter existing firms has to have demonstrated full compliance with protocol requirements during previous quarters
- **Data entry:** The Unit manages entry of export and import information into a QIZ trade database which supplies trade statistics to support policy discussions in Egypt-Israel QIZ Joint Committee meetings;

¹⁸ In 2009, a report prepared for USAID by Nathan Associates Inc. reviewed QIZ operations during an evaluation of labor skills constraints on QIZ factories See *Improving Productivity in Egypt's Ready-Made Garments Sector*, Marelllo, Salinger and O'Dell, Nathan Associates Inc., May, 2009

¹⁹ The number of registered QIZ companies actively exporting in December 2012 was approximately 250.

- **Compliance verification:** QIZ Unit compliance engineers make twice yearly visits to the export-active QIZ companies to evaluate their risk level and ability to satisfy origin verification requirements of U.S. Customs and Border Protection (CBP) and its Textile Production Verification Team (TPVT)²⁰ ;
- **Customer care:** the Unit confers with current and prospective Egyptian exporters regarding the eligibility of their products for QIZ benefits. It also maintains a business-to-business directory of potential Israeli partners and products including Egyptian suppliers of qualifying Israeli inputs.

This annual registration process involves approximately 850 companies and the quarterly activity reporting covers approximately 250 companies actively exporting from QIZs. The QIZ Unit was originally planned to use and at one time employed electronic data interchange (EDI) with its client producers for registration applications, quarterly reports, and registration renewals. After a server failure in 2010, transactions were converted to Excel spreadsheets received via email and uploaded manually, a less efficient and more work intensive arrangement. The Unit has never had vehicles or mobile data processing capability despite the need to travel to QIZ companies to conduct compliance audits, support QIZ Joint Committee meetings and assist the government in QIZ policy decisions.

BUDGETARY STATUS

Although the QIZ Unit is in the portfolio of the Minister of Industry and Foreign Trade, it is not included in the official Egyptian government budget. Mr. Sabry explained that the unit relies on funding from the Operational Unit for Development Assistance (OUDA), a UNDP special fund provided to the minister to cover personnel costs and operations. Mr. Sabry and Dr. Korani noted that the level of OUDA funding limits the QIZ Unit staff to core functions. Procurement and maintenance of equipment have been marginal. There is no allotment for training, and the unit has not expanded its role into attracting investment in the QIZs.

Long-term planning and budgeting are difficult given the uncertainties of annual development funding from OUDA and other ministerial-level demands on that funding. It is not clear that the support from OUDA will continue indefinitely.

QIZ WEBSITE

Additional information on the QIZ Unit can be found on its website, <http://www.qizegypt.gov.eg>.

²⁰ US CBP's Textile Production Verification Teams travel to countries whose garment exports to the United States are eligible for duty reduction under trade agreements or preference programs. Since access to reduced duties on garments is limited to a relatively small number of beneficiary countries, the TPVT confirms that the producers are actually making qualifying garments and that they are able to prove, through their production records, that the apparel was not produced elsewhere and illegally transshipped to the United States. During a 2012 visit to Egypt by the TPVT they found 7 of 21 companies visited were unable to fully document and substantiate the eligibility of their exports but it is not clear whether these companies were randomly chosen or were already known to the QIZ Unit as high risk based on their own compliance visits.