Egypt and Israel's Growing Economic Cooperation

by Haisam Hassanein

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Brief Analysis

Although security cooperation tends to get the headlines, the two countries have been quietly pursuing other initiatives that could provide a desperately needed boost to Egypt's trade, tourism, and energy sectors.

On October 18, Ynet news reported that Egypt and Israel were planning to pursue joint economic projects after years of cold relations on that front. Although officials are still ironing out the details, the announcement reflects the next stage in an economic relationship that has fluctuated considerably since the 1979 peace treaty. It also highlights how bilateral cooperation has expanded well beyond improvements in the security realm.

BACKGROUND

Formal economic relations between the two countries began in 1980. Once the peace treaty was signed, the Egyptian parliament approved the first trade agreement with Israel on May 8, 1980. Yet while joint committees were established to enhance engagement in various sectors, actual cooperation was kept to a bare minimum during the long rule of President Hosni Mubarak.

The turmoil that followed Mubarak's 2011 ouster further precluded the development of stable relations. Yet economic ties have begun to deepen under President Abdul Fattah al-Sisi, whose government faces worsening fiscal challenges and reportedly plans to move forward with initiatives on three fronts: the free-trade areas known as Qualifying Industrial Zones (QIZs), the tourism sector, and the energy sector.

BROADENING OF THE QIZ

This April, for the first time in ten years, an Israeli delegation traveled to Egypt to discuss ways of enhancing economic cooperation. Cairo was keen on increasing QIZ exports to U.S. markets and therefore welcomed Israel's help. The country's various QIZs -- located in the Greater Cairo area, Alexandria, the Suez Canal area, the Central Delta region, and Upper Egypt -- are home to more than 700 companies and employ around 280,000 workers. Currently, they account for 45 percent of national exports to the United States.

The protocol establishing the zones was signed in December 2004 as an extension of the U.S.-Israel Free Trade Agreement. At the time, the zones were critical to the survival of Egypt's textile industry -- the agreement came into force just as the World Trade Organization was removing relevant quota restrictions and signing preferential agreements with other nations.

Since then, however, Egypt has sought to reduce the Israeli input in the QIZs (i.e., the percentage of a given export product that must be manufactured by Israeli firms, based on a formula in the original agreement). Two rounds of talks have taken place toward that end. In 2008, Israel agreed to reduce its input from 11.7 to 10.5 percent. During the second round, which took place two weeks before the Muslim Brotherhood-led government assumed power in 2012, Israel verbally agreed to further lower its input but did not actually do so in practice. The issue was not picked up again until December 2015, when Israel reportedly handed Egypt another 2 percent of its QIZ share.

TOURISM

Following the 2011 uprising, Israeli tourism to Egypt witnessed a massive decrease, dropping from 226,456 visitors in 2010 to 133,620 in 2012. The numbers slowly began to recover thereafter, increasing to 140,425 in 2014 and 148,336 in 2015. Although the 2016 tally is of course not yet final, an estimated 15,000 Israeli tourists entered the country between January and March -- a comparatively small number that reflected the severe reduction in overall foreign tourism to Egypt after a Russian passenger jet was bombed the previous October. These numbers rose throughout the summer, however. Statistics from the Taba border crossing indicate that 14,270 Israelis crossed in June, then 29,000 in July and 45,000 in August, comparable to figures from last summer (around 90,000 Israelis traveled from Eilat to the Taba crossing between July and September 2015).

Indeed, thousands of tourists have continued to flock to Sinai beaches despite constant security warnings from Israeli authorities and frequent clashes between terrorist groups and the Egyptian military. In an October 25 report by Israel's Channel 2, for example, one tourist declared, "Being in Jerusalem is more dangerous than being in Sinai."

The one-sided nature of Israeli-Egyptian tourism remains a problem, though things are changing in this regard. In May, a delegation from the Egyptian tourism industry met with Israelis in Jerusalem and agreed to increase the number of Coptic Christians allowed to visit holy sites in Israel. For their part, the Israelis promised to increase the tourist flow to Egypt.

NATURAL GAS

In recent years, Egypt has moved from being a significant gas exporter to a net importer. This trend will likely continue even after the new supergiant Zohr field off Egypt's coast starts up next year.

Meanwhile, Israel has made its own large gas discoveries and is now a potential supplier to Cairo after years of importing Egyptian gas. These imports were once transported via a pipeline running across northern Sinai and along the seabed from al-Arish to Ashkelon, but various diplomatic, security, and economic factors brought the flow to a halt by 2012. Industry players have since proposed to reverse the pipeline, but efforts along those lines became embroiled in a $1.8 billion legal mess after the Israel Electric Corporation took Egypt to international arbitration for the 2012 cutoff.

The logical approach would be to convert supplies from Israel's offshore Tamar and Leviathan fields into liquefied natural gas at Egypt's Edku and Damietta plants on the Nile Delta and then export it by ship. Another possibility is to give some of the gas to Egyptian industries, since the government often diverts their supplies to fuel domestic power plants.

Buying Israeli gas would likely be just as politically contentious for Cairo as selling gas to Israel was in the past; the Egyptian media and intelligentsia remain hostile to the idea. But there are signs that authorities are preparing the ground for such deals. On October 27, an Egyptian appeals court acquitted Mubarak-era oil minister Sameh Fahmy of selling underpriced crude to Israel. In 2012, he had been sentenced to fifteen years in prison.

POLICY IMPLICATIONS

Since the 2011 uprising, Egypt has been running out of options to save its economy, as evidenced by its struggle to fix growing budget deficits, increasing unemployment, lagging tourism, and dwindling foreign direct investments. Even remittances by Egyptian expatriates -- the majority of whom live in Gulf Cooperation Council countries and whose money transfers are a major economic asset -- have decreased since the sharp fall in world oil prices. If these problems continue, the country will find itself on an increasingly dangerous trajectory, which is not at all in America's interest.

Even amid these negative trends, however, a positive bilateral dynamic has been developing. Three decades ago, Washington felt compelled to keep itself directly involved in managing the Egypt-Israel relationship. Nowadays, changing regional dynamics have allowed the two countries to move closer without a U.S. catalyst.

Given their deep security cooperation and Egypt's ongoing economic meltdown, the two neighbors might be on the verge of a new era of cooperation -- but only if they are willing to provide sufficient incentives to each other. Such a shift would fit well with Washington's broader interests in regional peace and stabilization. Accordingly, U.S. officials should encourage the latest Egyptian-Israeli initiatives and explore ways to further widen and deepen their economic cooperation.

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