

PALESTINE MONOGRAPHS

6

THE ARAB BOYCOTT
OF ISRAEL

MARWAN ISKANDAR



RESEARCH CENTER
PALESTINE LIBERATION ORGANIZATION

**THE ARAB BOYCOTT
OF ISRAEL**

THE ARAB BOYCOTT
OF ISRAEL

by

Marwan Iskandar



Research Center — Palestine Liberation Organization

Beirut — Lebanon

November 1966

TABLE OF
CONTENTS

	PAGE
I- INTRODUCTION	7
II- THE ARAB BOYCOTT IN INTERNATIONAL LAW	11
III- THE BOYCOTT - MAIN PROVISIONS AND ECONOMIC EFFECTS	23
IV- ECONOMIC OPPORTUNITY : ISRAEL V.S. ARAB WORLD	42
V- THE BOYCOTT EFFECTS ON THE ARAB WORLD	48
CONCLUSION	55

I. INTRODUCTION

The Arab Boycott of Israel has been subjected to severe criticism in the past few years. In northern Europe, the United Kingdom and the United States, there were attempts which aimed at soliciting governmental sanctions against trade with the Arab countries in lieu of the exercise by these countries of an economic boycott of Israel. To achieve this result, the propagators of sanctions against Arab countries forwarded two basic arguments; one aimed essentially at governmental authorities, the other at the general public in each of the Western countries concerned.

In the first instance, the nature of the argument stressed for securing governmental sanctions against Arab countries by western nations was legalistic. It was claimed that the Arab Boycott is in contravention of international legal principles and practices. Therefore, sanctions by advanced Western countries which adhere to the spirit of international law, were advanced as a natural corollary to the breach of international legal conduct assumed to exist on the part of the Arab countries exercising the economic boycott of Israel. To the surprise of anyone well acquainted with the facts pertaining to the Arab-Zionist conflict in Palestine and consequent developments, this argument was given

some consideration by practically all the Western countries where it was forwarded. The reactions which resulted have remained so far essentially threats of reprisal.

Members of the general public were influenced by a different sort of argument. To weterners, who by and large have come to cherish peace above everything else, the Arab Boycott was and still is pictured as an extention and manifestation of Arab military aggression against Israel. The Israelis attempt contineously to stress that the Arabs have maintained an attitude which is not conducive to peace. Consequently, the Israelis allege to the western popular opinion that peace cannot come to the Middle East unless the Arab countries restrict their belligerence. Those impressed with this argument have come to regard the Arab Boycott as an immoral practice. They press on their respective governments to give consideration to this breach of moral principles.

This study aims at clarifying the nature of the Arab Boycott and evaluating its effect on Israel and third parties. Despite the patent fallacity of both arguments fostered by the Israelis about the Arab Boycott, one finds it necessary to dwell briefly on these arguments before moving to the main purpose. This, we propose to do by discussing the legality of the Boycott in terms of international legal principles and practices and in reference to the

basic Armistice Agreements which continue to regulate the actions of the Arab countries and Israel.

The second argument concerning the immorality of the Boycott stands on whether or not the allegation that Arab countries exercise belligerent rights in contravention of principles of international law is true. It should not be assumed that legal and moral principles are one and the same. Far from it. But, this is one instance of intended confusion and it will be sufficient for our purposes to clarify the position of belligerent parties in international law.

II. THE ARAB BOYCOTT IN INTERNATIONAL LAW.

Appreciation of the Boycott's legality requires that it should be described in its historical origins. Early in the 20th century, the Arab population in Palestine began to suspect the motives of Zionist settlers. These were demonstrating a negative attitude towards the indigenous population. Zionist settlers did their best to achieve as high a degree of self sufficiency as was possible for an incoming minority. In agricultural settlements, the drive towards self sufficiency and non-cooperation with the indigenous population manifested itself in a partial boycott by the Zionists against the Arabs. This boycott which developed around 1907-1908, subsequent to the Basel Convention of 1897, took the form of prohibition of Arab employment in Zionist settlements and the purchase of agricultural products from the Arabs by Zionist settlers. But these acts produced localised reactions only, especially as the total number of Zionist settlers and Palestinian Jews represented by 1918 some 10 percent only of the total population in Palestine and owned around 2.5% of the land. Nevertheless, the use of an economic boycott as a tool for political ends was introduced into Palestine by the planned acts of Zionist settlers.

Arab suspicion turned after World War I into acute awareness of the drive by Zionist Jews to control Palestine. In 1917, Lord Balfour's promise that Britain would help World Jewry to establish a national home, coupled with the disclosure of the Sykes-Picot agreement by the new Russian regime, helped to increase the apprehensions of the Palestine Arabs, then 90 percent of the total population.

Zionist practices and increasing numbers of immigrants could not but cause the indigenous Arab population to view its own future with fear. Consequently, in 1936, the Arabs rose in violent opposition to the policy of open immigration for the Jews sanctioned by the mandatory authorities in Palestine. In the four preceding years, the rate of inflow of immigrants had increased from 9,500 in 1932 to 62,000 in 1935. This development was most significant to the Arabs in that the increase in Jewish population from immigration and natural birth in 1935 amounted to practically three times the increase in the Arab population. In absolute figures, whereas the Arab population then numbering some 960,000 increased by approximately 25,000, the Jewish population then numbering 290,000 increased by approximately 70,000.

It is no wonder that the Arabs around this time, having witnessed the proportionate increase of the Jewish population from 10% of the total population in 1918, to 28 percent in 1936, and the

latest triple rate of increase in the numbers of the Jews as opposed to their own, began to adopt measures which they hoped would prevent Zionist ambitions from being realized.

During World War II, immigration could not take place at the rate it had reached before the War. Moreover, as the Germans advanced in North Africa towards Egypt and Palestine, the Jewish population became restless and immigration practically came to a stand still during the first four years of the war. In consequence of these developments, Arab-Jewish conflicts subsided during this period. But by 1945, the Arabs, fearing a resumption of Zionist activities intended to secure control over Palestine, took an important step towards frustrating them. The Arab League, which had been formed in 1944, decided to begin an economic boycott of Jewish products in Palestine, with the object of retarding their industry and thereby weakening their power to establish a Zionist state in Palestine. This move is important in that the Arab League states which decided on this boycott were independent states taking an action intended to preserve the rights of the Arab indigenous population in Palestine which was still subject to the mandate system.

The Arab League states were acting in support of the Palestine Arabs who were prohibited from organizing para-military groups by the man-

datory power, in contrast to the freedom granted in this respect to the Jewish population. The only open alternative that was left for the Palestine Arabs to oppose Zionist designs was that of continuing their economic boycott of Jewish products which had started in 1936. They were supported in their renewed effort by the decision of the Arab League. Technically speaking, however, the Arab boycott of 1945 was not implemented efficiently.

In the wake of the Palestine War, The Arab League took a unanimous decision in May 1949 to establish boycott offices in all Arab countries under the supervision of a head office to be located in Damascus. By this time, the Arabs were trying to use the boycott to deny Israel the economic power to make further progress towards achieving its territorial ambitions. This is the background to the boycott which is alleged to be in contravention of international law. The allegation is based on the notion that the Arab Boycott represents the use of a right only granted to belligerent states during wartime. But, the argument continues, as the Armistice Agreements between Israel on the one hand, and Egypt, Jordan, Syria and Lebanon on the other were intended to lead to a peaceful settlement, continuity of the economic boycott contradicts the spirit of the Agreements and international law, in so far as these Agreements regulate outstanding matters between parties to the Palestine war.

At the 381st meeting of the Security Council held on November 16, 1948, it was resolved that; Council «... calls upon the parties directly involved in the conflict in Palestine, as a further provisional measure under Article 40 of the Charter, to seek agreement forthwith, by negotiations conducted either directly or through the Acting Mediator on Palestine, with a view to the immediate establishment of the armistice including: (a) the delineation of permanent armistice demarcation lines beyond which the armed forces of the respective parties shall not move: (b) such withdrawal and reduction of their armed forces as will ensure the maintenance of the armistice during the transition to permanent peace in Palestine»¹.

Between February 1949 and July 1949, Armistice Agreements were concluded successively between Israel and Egypt, Lebanon, Syria and Jordan. These agreements were novel in one respect. «It was implicit in the Security Council's approach to the problem that there was nothing even remotely approaching a victor and vanquished relationship between the parties, who were negotiating upon the basis of absolute political and military equality»².

-
1. Rosenne, Shabtai, *Israel's Armistice Agreements With The Arab States — A Juridical Interpretation*, (Blumstein's Bookstores Ltd., Tel Aviv, 1951) p. 22.
 2. *Ibid.*, p. 31.

By contrast, in all modern precedents, armistices were dictated by the victor and not negotiated.

Due to the negotiated character of the Armistice Agreements between parties exercising equal rights, it was an essential pre-requisite to restrict the military operations of all parties. The Armistice Agreements were to stand or fall on adherence by the parties involved to the terms restricting military operations. If violations were to be serious and numerous, then one could not expect the Armistice Agreements to be provisional measures leading to permanent peace.

The importance attached to the aim of preventing military aggression is manifestly clear in the Armistice Agreements. «The Egyptian, Lebanese and Jordan Agreements contain an identical Article I laying down four principles to be fully observed by both parties during the armistice. This was done with a view to promoting the return of permanent peace in Palestine and in recognition of the importance in this regard of mutual assurances concerning the future military operations of the parties»³. In the Syrian agreement, the text was slightly modified without any substantive changes.

In their respective order, the four principles referred to were:

3. Ibid., p. 42.

«1. The injunction of the Security Council against resort to military force in the settlement of the Palestine question shall henceforth be scrupulously respected by both parties.

2. No aggressive action by the armed forces — land, sea or air, of either Party shall be undertaken, planned or threatened against the people or the armed forces of the other; it being understood that use of the term 'planned' in this context has no bearing on normal staff planning as generally practised in military organizations.

3. The right of each Party to its security and freedom from fear of attack by the armed force of the other shall be fully respected.

4. The establishment of an armistice between the armed forces of the two Parties is accepted as an indispensable step toward the liquidation of armed conflict and the restoration of peace in Palestine»⁴.

It is clear that the first three principles constitute the corner stone in each of the four Armistice Agreements that were concluded. The fourth principle is no more than a logical legal conclusion that obtains in case the first three principles are meti-

4. Ibid.

culously observed. Moreover, it is an accepted principle in international law that «Armistice» does not signify termination of the state of war between belligerent parties. To any state involved in war, the state of war does not end in respect of its international legal ramifications until that state agrees to such termination of its own free or forced will.

Already we have noted that the Palestine war produced nothing like a victor-vanguished relationship. Consequently, termination of the state of war between the signatories of the Armistice Agreements had to depend on decisions taken by their own free will. The Arab countries were given no opportunity by constant Israeli aggression in violation of the Armistice Agreements to decide on termination of the state of war.

To substantiate this interpretation of events subsequent to signature of the Armistice Agreements it is sufficient to stress few salient features of Israel's military violations by contrast to military actions by the Arab states. It is important to recollect at this point that military action in violation of the Armistice Agreements constitutes an outright abrogation of international legal commitments. For the purpose of lessening strain between the parties to the Armistice Agreements three areas were delimited and declared as non-military or de-

militarized zones. No military actions or movements or personnel were to be allowed in any of the demilitarized zones.

Against this background made absolutely clear to Israel and the Arab states, Israel:

1. Undertook the planning and execution of organized military action in violation of all the principles of the Armistice Agreements.

2. Transgressed over parts of all the demilitarized zones, and despite censure by the Security Council and General Assembly still violated, on what seems to be a continuing bases, areas of two of the three demilitarized zones.

3. Achieved the highest rate of international criminal delinquency as between all states, members and non-members of the United Nations, since it became obliged by international agreements to strive towards maintaining peace.

By contrast, not one Arab state has been censured for military action in violation of the Armistice Agreements. Had it not been for Arab adherence to the spirit of the Agreements, and effective, though in many instances, belated interference by the organs of the United Nations, widespread war would have erupted in the Middle East.

The status of tension perpetrated by Israeli aggression and intended oblivion to international obligations cannot be interpreted in any way as progress towards a peaceful settlement over Palestine. Consequently, the Arab view that a status of war still exists and warrants the exercise of an economic boycott against Israel is perfectly in line with the principles of international law.

This view is supported by the implicit admission at the time of negotiation of the Armistice Agreement between Syria and Israel that the former had the right to exercise an economic boycott against Israel without this action leading to any violation of the Armistice terms. At no point in the Armistice Agreement do we find explicit reference to the Boycott. Yet, the Armistice Agreement between Syria and Israel was finally signed on July 20, 1949, long after the establishment of the Head office for the Arab Boycott in the capital of Syria in May, 1949. Had the boycott been in violation of the Armistice Agreement, surely explicit reference ought to have been made to that particular.

In view of the above arguments, it is clear that the Arab Boycott of Israel is an act that conforms to international legal principles. As a matter of fact, the Arab states in view of Israel's actions would have been entitled to military reprisals and neglect of the Armistice Agreements' terms. That

the Arab states have chosen to exercise the least belligerent of their international legal rights to curb Israeli aggression is a clear testimony of their collective good will and adherence to international law.

III. THE BOYCOTT — MAIN PROVISIONS AND ECONOMIC EFFECTS.

The Boycott has two complementary aspects, a positive one and a negative one. The negative one was aimed at preventing direct or indirect exports to Israel of Arab products or imports from Israel by Arab countries. In cases where Israel might try to get to Arab markets as a buyer or investor through other countries or persons, there are detailed regulations to prevent this from happening.

In its positive complimentary aspect, the Arab boycott of Israel aims at preventing capital from flowing into Israel and persuading already invested capital to leave, competing with Israel in its export markets and creating difficulties for Israel when it tries to secure materials needed for its industry.

Realization of either of the two general aims of the Arab Boycott requires the implementation of detailed provisions by all the Arab League countries. We shall not deal with each and every provision, but will touch on those provisions that are especially relevant to third parties. And this will be done in the context of discussing the economic effect of the boycott on Israel.

It is very hard to assess what effect the Arab Boycott has had so far. The difficulty springs from

the approach which has to be followed for providing quantitative indicators. From a static approach, which is the only one open to us, the effect of the boycott must be assumed to equal the difference between economic conditions in Israel at present and what these conditions would have been in the absence of the Boycott. Due to the inherent difficulty of this calculus we shall try to supplement this approach with plausible hypotheses about the channels through which the boycott affected Israel's development. Also, changes in effect due to changing circumstances over time will be noted.

Any economy has fundamental problems which reflect its endowment of natural resources and the resourcefulness of its inhabitants. In respect of natural resources, Israel is fairly poor. Not more than 25 percent of the land is cultivable and of this only 35 percent is under irrigation. Water resources have been fully utilized and not much more can be devoted to increasing agricultural production unless a cheap method of distilling sea water is developed. Mineral resources on the other hand are very few and of limited importance. These include copper found at temnah in Southern Negev in small quantities, potash at Sedom in Northern Negev, Bromide, which is a potash residual, and phosphates. Asphalt and sulphur are found in quantities sufficient to meet local consumption. Oil production amounts to 200,000 tons a year and covers 7 — 8

percent of requirements. Of late, natural gas production has increased to 73 million cubic metres in 1965. Most of this gas is utilized as fuel at the Dead Sea works and the Oron phosphate Plant ⁵.

It appears that in the absence of further discoveries of mineral resources or a cheap method of distilling sea water and there is little hope for either in the near future as strenuous efforts sustained in both directions in the last decade led to little success, Israel's agricultural and mineral production are not likely to increase at a fast rate. Agricultural production has failed to keep up with the growth of other sectors in the economy. Moreover, the growth in population and per capita consumption of food just exceeded the 50 percent growth in agricultural production in the past eight years.

Israel has committed itself to a policy of unlimited and unselective immigration into the country by Jews from all over the world. Together with this undertaking, Israel is committed to be a welfare state. Consequently, government authorities are under strict obligation to provide new immigrants and the unemployed with relief payments. Also, jobs have to be created for absorption of new immigrants in productive employments.

5. Bank Leumi's — *(Review Of Economic Conditions In Israel, special Issue, July 1966, p. 28.*

These policy commitments led under pressure of mass immigration between 1948 and 1951 (Net immigration: 1948 — 104, 480, 1949 — 234, 922, 1950 — 160, 160, 1951 — 166,859) to inflationary pressures reflected in a depreciation in the exchange value of the Israeli pound from IL 1 = \$4.05 to a rate of one to one applied to certain transactions in February 1952. Later, the rate depreciated further to IL 1.08 to the dollar in 1960⁶. Influx of immigrants and lax fiscal policies contributed to further worsening of the exchange rate of the Israeli pound. By 1965, the official exchange rate was IL 3 per U.S. dollar. But the pressure towards a less favourable rate was still great despite the deflationary situation in Israel during 1965. Free market rates were about IL 3.30 per dollar, although for a short period the rate was as high as IL 3.45⁷.

Due to Israel's capital requirements for developing its economy and its inability to achieve self-sufficiency in the production of food and raw materials, Israel has had to face a wide gap in its balance of payments on current account. In spite of this, Israel developed at a fast rate between 1948 and 1965. Population increased 3 3 times, while in-

6. Iskandar, M. «The Arab Boycott of Israel», *Middle East Forum*, issue of October 1960, p. 27.

7. Op-cit., p. 15.

dustrial and agricultural production increased more than 3.5 times. Such developments are inexplicable except for a continual flow of aid. The principal sources of aid were gifts and long term loans from American Jewry, grants in aid, technical help and food surpluses from the American government; and, from 1958 on, reparations payments in the form of goods and services from West Germany. More recently, foreign investment has come to account for substantial inflow of capital.

The problem discussed has been well summarized by Dr. Yusif Sayegh, in a paper entitled **THE ISRAELI ECONOMY IN THE BALANCE**⁸. «The levels of consumption and investment which Israeli authorities chose for the country call for resources that are far beyond what the economy is able to produce. Not wanting to lower these levels, the authorities have continuously fallen back on sources of foreign aid to meet the deficit between total resources needed and resources produced domestically... «Year in and year out the Gross National Product in Israel has on the average amounted to 82.3 percent of total resources available, in a range that stretches between 79.8% (1956) and 85.5% (1958) i.e., the import surplus (foreign aid and the

8. Delivered as a public lecture at the American University of Beirut in 1962.

like) ^x has on the average been 17.7% of total resources, or a fourth of GNP. Net investment, all of it, has been made possible through donations and capital movements into Israel. This does not mean that the Israelis have not saved anything out of GNP: it means that they have consumed (and depreciated their productive goods) to the equivalent of all their GNP». Up till now, Israel continues to depend on donations and capital movements for maintaining its growth, which, however, has slowed considerably in the past year.

To have a better perspective of Israel's dependence on capital movements and donations for sustaining the standard of living of its population, it is instructive to view the balance of payments' position in 1964 and 1965.

x. (Insertion by writer.)

TABLE I
ISRAEL'S BALANCE OF PAYMENTS 1964 AND 1965 (in \$ MN).

Item	1964		1965	
	Income	Expenditure	Income	Expenditure
Current Account				
Imports	—	741.6	—	733.0
Exports	349.4	—	403.4	—
Transport, tourism & insurance	187.6	186.7	213.5	206.1
Interest payments and receipts	28.7	93.8	36.8	105.5
National funds and public institutions (incl. transfers in kind)	100.2	4.3	103.3	4.1
American grants-in-aid	8.2	—	4.7	—
German reparation payments	22.8	5.9	19.8	3.1
German restitution payments	134.2	—	112.7	—
Private transfers	97.1	1.2	108.5	1.4
Government, n.e.s.	21.1	98.6	20.8	130.7
Miscellaneous	32.4	67.8	36.9	57.2
Total	981.7	1,199.9	1,060.4	1,241.1

Ctd...

TABLE I B/F

Capital Account					
Foreign investments (net)	156.7	13.8	98.0	5.8	
Independence and Development Bonds	98.7	74.2	100.4	67.1	
Loans from the U.S. (including loans for the purchase of agricultural surpluses)	58.9	27.2	81.0	6.2	
Export-Import Bank loans	9.7	21.1	8.0	23.5	
World Bank loan	12.6	0.1	23.5	0.4	
Other medium and long-term loans	115.6	62.5	103.2	56.1	
Short-term loans	—	5.6	62.7	—	
I.M.F.	—	6.2	—	—	
Foreign currency balances & monetary gold	4.2	25.5	—	106.0	
Miscellaneous	7.6	0.2	10.5	3.3	
Total	564.0	236.4	487.3	268.4	
Errors and omissions		9.4	—	38.2	
Grand total	1,445.7	1,445.7	1,547.7	1,547.7	

Source : «Review of Economic Conditions in Israel», op. cit., p. 12.

The commentary on the importance of grants in aid and capital inflow to Israel's economic conditions contained in the quoted review reads; «Once again the deficit in the balance of payments on current account was more than offset by the flow of unilateral transfers and capital imports, although the total inflow declined by \$ 8 million to \$596 million in 1965. Of the unilateral payments, German reparations contributed \$17 million as in 1964. Personal restitution payments from Germany to individuals which reached a peak of \$113 million in 1963, and totalled \$134 million in 1964, declined to \$113 million in 1965. The drop in such transfers in 1965 was due to the dwindling of lump sum payments, whilst restitution pensions flowed in at much the same pace as in 1964. Restitutions are expected to remain at the same level in 1966, but in the future receipts should increase due to new German legislation which extends the categories of persons eligible for such benefits»⁹.

In spite of the magnitude of reliance on foreign aid and foreign capital portrayed in the figures of TABLE I, the importance of these items to Israel's development is even greater. This is so because agricultural possibilities are utilized to the greatest extent possible and Israel has found it necessary to shift its emphasis in production to industry.

9. Ibid., p. 13.

Lacking the raw materials required for a diversified industrial base Israel has had and continues to import most of the raw materials utilized in its industry. In fact, raw materials and fuel imports (the largest proportion of which is utilized in the production for export of petroleum and petrochemical products) accounted for 67 percent of Israel's total commodity imports in 1967. This high proportion of raw materials imports which in turn makes possible a high level of industrial exports, which accounted in 1965 for 77.7 percent of Israel's total exports, would not have been within Israel's potential if not for grants in aid, foreign borrowings and foreign investments.

Future development must rest, as in the recent past on the availability of economic resources produced abroad, and made available to Israel on fairly easy terms. The Arab Boycott, if it is to have a significant effect on retarding Israel's growth, should exercise an adverse effect on one or more of the main constituents of the resources available to Israel from other countries. At present there is open opportunity for the Arab countries to utilize their privileged position as the major suppliers of free capital on the world markets to press their purpose. This is all the more important as the avenues through which the boycott affected Israeli development previously are now partially closed. We shall discuss these later and turn now to ex-

plore the means open for the Arab countries to limit the import surplus that has enabled Israel to develop at a fairly fast rate.

There are three important items in the constituents of Israel's import surplus which are not amenable to Arab pressure nor subject to economic rational. These are; Loans from the U.S; proceeds from the sale of Israel independence and development bonds essentially on the American market and German restitution payments. In respect of the first item it is likely that American aid will continue, and in fact, increase as the pressure by Arab countries to tighten the boycott increases. Sale of Israel independence and development bonds depends on the enthusiasm continuously maintained for Israel amongst a large segment of American Jews. German restitution payments are affected mainly by political considerations.

While Arab efforts to tighten the boycott are not likely to achieve positive results in respect of the three items noted above, much success can be expected on account of the remaining items. These can be divided into two categories: Foreign investment and long term loans by international institutions. To attract foreign investment a country must have special institutional and natural advantages. Also, the scope for selling products on the home market must be substantial and/or supplemented by export opportunities.

Israel has precious few natural advantages; its market is fairly limited; its economy by virtue of government political commitments and lax fiscal policies portrays structural inflationary pressures, and its foreign exchange position, measured in terms of the ratio of foreign debt retirement and interest payments to total foreign exchange earnings, worsens every year. Moreover, the natural geographical markets for exportable products are the neighbouring Arab countries which prohibit any exchange of goods.

The boycott regulations stipulate that companies having regional offices or direct investments in Israel shall not be allowed to operate in Arab countries and their products will not be allowed to enter these countries. Companies which have to have a regional office in the area have established their offices in Arab countries — usually Lebanon — and have come to appreciate the attendant advantages. Arab markets are far more important than Israel's market for practically all kinds of consumer and producers' products and services.

It becomes fairly clear from the above discussion that, except in minor instances where demand for a particular product whether it be a good or service is much higher in Israel than it is in the Arab countries, foreign investment in Israel is not likely to be an attractive proposal. The strength of

this argument becomes far more persuasive when a foreign investor stops to consider the advantages which foreign investment reaps in the Arab world in contrast to the restrictive possibilities in Israel. Before elaborating on this aspect, it is useful to consider two further possible causes for investing in Israel, especially as the second of the two is strongly linked to the comparative calculus stressed above.

Labour productivity in Israel could be much higher than labour productivity in industrial countries, and thus compensate for costs of transport of products from Israel to these countries and tariffs imposed on these imports. But, we find that labour productivity in Israel is lower than productivity of labour in the industrialized countries of Western Europe. Moreover, wages in Israel are linked to the cost of living index which rose very fast with inflationary pressures. In consequence of these considerations, and the high import content of Israeli exports, foreign investment cannot expect, other than in minor instances, to capitalize on any advantage in Israel's labour market.

Finally, institutional factors might tempt foreign investors. Israel tried to overcome the major disadvantages which confront foreign investment through promulgation of the law of the Encourage-

ment of Capital Investment 1957 — 1959¹⁰. Article I of Chapter One of the law defining its object, reads: «1. The object of this Law is to attract capital to Israel and to encourage economic initiative and investments of foreign and local capital with a view to —

1. The development of the productive capacity of the national economy, the efficient utilization of its resources and economic potential and full utilization of the productive capacity of existing enterprise;

2. the improvement of the balance of payments of the State, the reduction of imports and the increase of exports;

3. the absorption of immigration, the planned distribution of the population over the area of the State and the creation of new sources of employment». But the detailed exemptions granted of various duties and charges as well as a reduced rate of income tax do not compensate for the inherent disadvantages that face foreign investments in Israel.

10. The text of the Law and later amendments appears as Appendix I in; Marcus, Ernest, *Investment In Israel* (C.W. Leske Verlag Opladen, Germany, 1966) p. 123.

We have noted already The Arab Boycott regulations which prohibit commercial dealings with business enterprises that have direct investments in Israel. By way of comparison, three Arab countries at least (Lebanon, Jordan and Kuwait) offer institutional legal benefits which equal or exceed those provided in the Law for the Encouragement of Capital Investment in Israel as amended. Furthermore, commercial agreements between the Arab countries facilitate the exchange of industrial products and apply reduced rates of tariff on goods produced in Arab countries. Consequently, investment in the Arab countries as opposed to Israel enjoys numerous advantages that relate to the extent of the market and institutional factors.

After diverting to discuss briefly the second categorie of capital inflow (long term loans from international institutions) which is amenable to reduction as a result of wider recognition of Israel's subsidised economic structure, a limited comparison will be drawn between opportunities open for co-operation with the Arab countries and Israel.

International financial organizations which offer aid for development purposes, like the International Bank and its various agencies, usually request that certain fiscal and/or investment policies be implemented before the grant of aid. In the case of Israel, however, international financial organi-

zations choose to demonstrate greater tolerance than has been demonstrated towards most other developing countries in greater need for long term loans. TABLE II illustrates the extent of foreign credit available to Israel. The table incorporates independence and development bonds with foreign loans. These figures were maintained as foreign lenders need to note the total of Israel's foreign obligations.

TABLE II
GOVERNMENT AND GOVERNMENT GUARANTEED FOREIGN
CURRENCY INDEBTEDNESS IN ISRAEL.
(In \$ Million)

	31.12.63		31.12.64		31.12.65		Increase in 1965 over 1964 in \$ mn.
	in \$ mn.	%	in \$ mn.	%	in \$ mn.	%	
Independence and Develop- ment Bonds	475	56	499	48	532	44	33
Other long-term loans (5 years or over)	254	30	420	41	525	44	105
Medium-term loans (1-5 years)	71	8	55	5	40	3	-15
Short-term loans (up to 1 year)	54	6	59	6	109	9	50
Total	854	100	1,033	100	1,206	100	173

Source — Review of Economic Conditions In Israel — 1966 — p. 14.

The International Monetary Fund developed from its experience over the years a criterion for judging the capacity of developing countries for foreign borrowings. It is judged by the Fund that any country which faces foreign debt amortization and interest payments which exceed 15 percent of its capacity to earn foreign exchange is in serious trouble. Israel has exceeded this limit and is in fact one of the most heavily indebted countries in the world. International agencies which overlook this fact, and more importantly, that Israel abstained from taking deflationary measures in order to stop the increase in its foreign indebtedness until very recently, prejudice the opportunities of other developing countries with greater need for international financing and readiness to abide by sound fiscal policies. In the interest of world monetary stability and the development of depressed countries, financial resources made available to Israel by international agencies should be limited from now on.

IV. ECONOMIC OPPORTUNITY :

ISRAEL v.s. ARAB WORLD.

Foreign businessmen and business organizations have to balance between opportunities in Israel as opposed to potential in the Arab countries when their decisions involve the activation of the Arab Boycott against them. Export opportunities from Israel are fairly limited due to reasons already discussed. And labour productivity and wage rates are not attractive in themselves when compared with productivity and wages in industrialized countries with whose products exports from Israel have to compete. Consequently, if new foreign investment is to be remunerative in Israel, it must be based essentially on local market demand for products imported at present. There are of course, other considerations, such as the total demand for a particular product in the country which need not be imported, and which might attract the foreign investor. But, foreign investment for the local market is not encouraged in Israel, unless it leads to import substitution on a substantial scale.

Against this background, it seems that opportunities for foreign investors in Israel as opposed to the Arab countries must depend first and foremost on the volume of imports and the opportunity for import substitution industries. It is clear that

on this basis, opportunity is far greater in the Arab countries than in Israel.

Our discussion, however, will not stop at this point. In order to emphasize the preponderant importance of the Arab countries in this respect, TABLE III provides a breakdown by geographical areas of Israel's imports as compared to the imports of two Arab countries, Lebanon, and Kuwait. The choice of the two Arab countries is not haphazard. These countries are amongst the most prosperous in the Arab world and more importantly, their combined populations amount to 2,600,000 which is the approximate total population of Israel.

TABLE III.**ISRAELI IMPORTS COMPARED TO
LEBANESE & KUWAITI IMPORTS IN 1964.****(In \$ Million)**

Source of Imports	Israel	Kuwait & Lebanon
U.S.A.	207.7	83
E.E.C.	240	212
E.F.T.A.	202	220
Japan	7.2	50
Rest of the world	166.3	272
Total	822.5	837

Sources: Review of economic conditions in Israel, 1965; State of Kuwait Statistical Abstract, 1965, and the Lebanese Yearbook of Foreign Trade Statistics, issued by the Custom's Board.

TABLE III provides an incomplete picture which needs to be punctuated with supplementary facts. Lebanese and Kuwaiti imports which exceed Israel's total imports are only 15 percent of total imports by Arab League countries adhering to the Arab Boycott. For example, American businessmen whose total exports to Israel in 1964 amounted to \$207.7 million, exported to the Arab countries in the same year goods valued in excess of \$600 million. Moreover U.S. exports to Israel were essentially raw materials which indicate no new opportunities for investment.

Aside from these considerations, foreign investment in Arab countries has additional advantages when compared with the disadvantages that accompany investment in Israel. During the coming decade, Arab markets will continue to grow at a fast rate with the growth of oil revenues that come about from increased production and better financial terms. By contrast, Israel's growth and accretions to its demand will continue to depend largely on foreign aid. Moreover, Arab businessmen have the capital to participate with foreign enterprise, not only in the Arab world, but also in the countries of foreign entrepreneurs.

To sum up, foreign investors must foresake Arab markets if they are to invest directly in Israel. They lose by such action a market that is far

greater than the Israeli market and overlook important possibilities for channelling Arab capital into their own countries. Trade with Israel will continue to be in the nature of sales on advanced credit, whereas the majority of the Arab countries are in a position to accomodate their imports from their own resources and still have enough capital to spare for Western capital markets. Finally, already discovered natural resources in the Arab world (other than petroleum) are in themselves a source of great attraction for foreign investors.

V. THE BOYCOTT EFFECTS ON THE ARAB WORLD.

Israel tries to create an impression that the Arab Boycott is disadvantageous from a development point of view to the Arab countries implementing it. This is so, the argument runs, because the Arabs would do better to rely on Israeli skills and the Israeli market. There is no truth in this argument, as will become clear from reviewing the Boycott effects on the Arab countries.

With the implementation of the boycott, the Arab countries found themselves cooperating to execute a common economic policy. As a direct by-product of this experience, the Arab Boycott head office in Damascus forwarded a proposal for the establishment of an Arab Common Market in 1953. The Common Market has not been achieved, but the way has been paved with agreements stipulating preferential treatment for Arab products as between signatories of agreements sponsored by the Arab League. It is important to emphasize at this point how much the joint effort in implementing the Boycott affected the development towards an Arab Common Market.

Progress towards a Common Market between the Arab countries has been very slow in relation

to complete elimination of tariffs as between themselves, and the setting up of a common external tariff. But, significantly enough, and in contrast to the slow progress witnessed in the purely customs characteristics of a common market, cooperation between the Arab countries has brought about free mobility of labour and capital as between most of them. From an economic point of view, this is more important than the lowering of tariffs and elimination of trade barriers.

Free mobility of capital and labour between most Arab countries could not have preceded less important forms of cooperation, such as elimination of tariffs, had it not been for the experience of cooperation in implementing the Arab Boycott. This is not to say that the Boycott led to free mobility of labour and capital, but it certainly did contribute towards widening and strengthening this trend. The Boycott produced a strong drive for development among the Arabs.

Facing the threat of Israeli expansionism, the Arabs associated in their minds power with economic strength. They implemented the Boycott to limit Israel's power and consequently its capability to expand, but by so doing, created a sense of the need for functional cooperation amongst themselves. The result of this has been wider integration of efforts towards development.

Labour and capital mobility led to greater diffusion of wealth generated by oil discoveries. Human skills travelled freely in the Arab world and educational trends began to reflect a general feeling that the Arab countries provide a natural habitat for any skilled Arab. This trend gained strength from differences in human endowments as between Arab League countries. Specialized Arabs who went to work in other Arab countries faced no difficulties like the ones faced today by European migrant labour in other European countries. Consequently, labour mobility in the Arab countries was very great and led to substantial mobility of capital. This fact provides the major explanation of the rapid rates of growth witnessed in most of the Arab countries during the past decade. To the extent that the Arab Boycott fostered this trend, it has been instrumental in pushing ahead the process of economic development in the Arab world.

There are other benefits which have accrued to some Arab countries from the Boycott. In 1948, the port of Haifa had better facilities than that of Beirut, and was more favourably situated for transit trade with Jordan and Saudi Arabia. No goods passing through Israel are allowed into the surrounding Arab countries nor are any ships allowed to visit an Arab port and an Israeli port on the same voyage. Planes bound for Israel are not per-

mitted to pass over any Arab countries. Under these circumstances, the exporting and importing of certain Arab countries which lacked the necessary facilities, have had to be carried out by another Arab country. Being most favourably situated among the Arab countries, Lebanon virtually inherited the greater part of the Palestine trade transit business. With the growth of trade between the Arab world and industrialized countries new sea ports were constructed in Jordan, Iraq and Saudi Arabia. These took away some of the benefit Lebanon had reaped, but in the meantime, a free trade area had been developed in the port of Beirut. Business carried in the free trade area, together with imports for Lebanon and for transit purposes still contributes to the prosperity of the country.

The boycott brought about similar developments in respect of Beirut and Damascus airports. Both airports, especially the former, prospered and expanded rapidly. International air traffic between Asia, Africa and Europe runs through either one of these two airports. Were it not for the Boycott, the flow of traffic could have gone through Tel-aviv.

For similar reasons, pipelines from Saudi Arabia and Iraq to the Mediterranean were extended through Syria and Lebanon in order to bypass the Israeli controlled lands. Oil transit royalties,

oil export dues, refinery taxes and supplies of petroleum products at prices lower than world market prices were few of the benefits that accrued to Lebanon and Syria.

Benefits from developments noted, went beyond the monetary income they brought to some Arab states. Principles of modern technology and organization became more widespread in the Arab countries. Employment opportunities widened and incentives were potent in directing efforts towards improving economic conditions in general.

In part, the Israeli claim referred to at the beginning of this section, stressed the loss suffered by the Arabs from not utilizing Israeli expertise. Knowledge of the background to the Palestine conflict is sufficient to explain the great resentment Palestinian Arabs feel towards the usurpation of their lands. This resentment is no less acutely felt by non-Palestinian Arabs and it is inconceivable to suggest that benefit can come about from reliance by those Arabs on Israeli services. Human motivation has been the source of success or failure of economic development in most countries. In the Arab world the resentment felt towards Israeli aggression helped to spur efforts. The Boycott, as a concrete manifestation of Arab resentment, and as a psychological drive, contributed positively to

greater welfare. Moreover, the Arabs have utilized every occasion to draw on foreign expertise from industrialized countries far more advanced than Israel. It is therefore, impossible to accept the Israeli claim that the Arabs have prejudiced their development by foresaking reliance on Israeli technicians.

The question might arise: is it not possible for the Arabs to benefit from exporting to Israel ? A definite answer is that no such benefit could arise. No more than 10 percent of Israel's imports at present could be imported profitably (to Israel) from the Arab world. There is demand for Arab products which Israel could benefit from by other Arab countries. If production of the particular food items and raw materials in question were increased, some Arab countries would absorb this increase by decreasing their imports of same from non-Arab countries. In brief, the potential for inter-Arab trade exceeds the volume of exchange at present. The problems facing Arab countries in overcoming development obstacles are not essentially represented by lack of export markets.

CONCLUSION

It was clearly demonstrated that the Arab Boycott is not in contravention of international law. Arab states have a perfect right to exercise an economic boycott against Israel. Actions by Israel in overt violation of international agreements left no scope for constructive progress towards peace. A state of war continues between the Arab League countries and Israel and justifies the boycott.

Foreign countries and business firms must give due consideration to the legality of the Arab Boycott. They should appreciate that its foundation is in the preservation of human rights, and that the Arab countries have manifested exemplary behavior in the face of continual Israeli aggression. The Arab Boycott, short of actual open fighting, has proven to be the most effective weapon in the hands of the Arabs for combating Israel. Governments and institutions which pay no heed to this fundamental security requirement, from the Arab point of view, must face the consequences of losing the growing Arab market.

It is our opinion, explained at length in this study, that much is lost and little is gained by neglect of the Arab Boycott provisions. On humanitarian and/or legal grounds, the Arab Boycott is justified and not only requires adherence to its provisions, but also rewards such regard.

Printed by
GHORAYEB PRESS
Beirut

RESEARCH CENTER
PALESTINE LIBERATION ORGANIZATION

606 Sadat Street (Apt. 22)

BEIRUT - LEBANON

Established in February 1965

Publications

- I. Palestine Chronology Series
- II. Facts and Figures Series
- III. Palestine Essays Series
- IV. Palestine Monographs Series
- V. Palestine Books Series
- VI. Palestine Maps Series
- VII. Special Publications