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THE IMPACT OF ANTI-BOYCOTT LAWS
ON U.S. MIDEAST TRADE

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The American Jewish Committee
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The Impact of Anti-Boycott Laws on U.S.-Mideast Trade

The Israeli-Egyptian Peace Treaty signed on March 26, 1979 commits Egypt and Israel "to remove all discriminating barriers to normal economic relations and to terminate economic boycotts of each other..." Egypt's formal withdrawal from the League of Arab States' long-standing boycott of Israel is a major step in a gradual erosion going on for some time, an erosion hastened by U.S. action to prohibit most forms of American compliance with the boycott, particularly the enactment in 1977 of comprehensive anti-boycott amendments to the Export Administration Act. Thus, though certain Arab states have vowed to continue their boycott against companies doing business with Israel, its effectiveness has been significantly undermined.

When the 1977 anti-boycott legislation was being debated in Congress, segments of the business community with close ties to the Arab nations issued dire warnings about its potential effect on trade with the Middle East. For example, Dresser Industries of Dallas, Texas bought two full pages in the Wall Street Journal (April 14, 1977) to predict that "500,000 jobs hang in the balance as Congress considers more boycott legislation." It is interesting, therefore, to examine the effect of the new laws after two years of operation.

Since the passage of the anti-boycott legislation, Dresser Industries itself has been tallying record revenues. Nor is Dresser an exception. U.S. trade with the Arab nations has risen to unprecedented levels over the past two years. At the same time, the more repugnant aspects of the extended Arab boycott have been sharply modified, if not eliminated.

Deputy Assistant Secretary of Commerce Stanley J. Marcuss summed up the situation in a Chicago speech on September 14, 1978:

Last year's gloomy predictions that passage of the foreign boycott provisions of the Export Administration Amendments would cost thousands of U.S. jobs and severely damage U.S.-Arab trade have not materialized. On the contrary, since the passage of the law, there has been a significant increase in U.S. exports to the 14 Near East/North African boycotting nations,

Secretary of Commerce Juanita Kreps made the same point in an address in New York City on November 21, 1978:

When the law was first enacted in 1977, there were some who predicted that it would have a disastrous impact on our trade. There were some who said that this nation could not afford to stand up for what was right because the economic cost would be too high. They were wrong.

Even Burhan Dajani, Secretary General of the General Union of Arab Chambers of Commerce, Industry and Agriculture, acknowledged to a Washington business conference in April, 1978 that "business on both sides has been able to live with these laws. It has been possible to continue the flow of trade."

Certainly 1978 trade figures confirm these views. U.S. Department of Commerce data show that U.S. exports to the 14 Arab nations which participate in the anti-Israel boycott reached \$8.36 billion in 1978, a 16.6 percent increase over \$7.15 billion in 1977. Moreover, the 1977-1978 increase was higher than that of the previous two years. (See Table 1.)

U.S. exports to the Middle East have shown healthy gains for several years in both absolute terms and in relative share of the market. Petroeconomic File (July, 1978), calculating the Middle East market shares held by Western European and North American exporters on the basis of IMF trade statistics, concluded that the U.S. market share rose steadily from 22.2 percent in 1973 to 26.2 percent in 1977. (See Table 2.) In the same period, France, probably the most pro-Arab member of the European Economic Community, suffered a steady decline in its market share -- from 28.7 percent in 1973 to 19.8 percent in 1977. Perhaps even more ironically, the three most zealous supporters of the boycott -- Libya, Syria and Iraq -- increased their imports from the U.S. by 34 percent in 1978, a rate double that of the Arab world as a whole.

Libya is one of this country's fastest-growing export markets, purchasing a total of \$425 million in 1978, 35 percent more than the record \$314 million in 1977 and up sharply from \$277 million in 1976 and \$231 million in 1975.

Our exports to Syria in 1978 rose nearly 7 percent over 1977, reflecting her partial recovery after a period of economic difficulty. The U.S. has sold Syria some \$272 million in goods and services in 1976; but these purchases dropped sharply because of severe economic problems arising from her intervention in Lebanon, and a decrease in aid from Arab states. Syria's economy grew 13 percent annually from 1973 through 1976, largely because of an unprecedented boom in the construction

TABLE 1. U.S. Exports to 14 Arab States, 1975-78

(in millions of U.S. \$)

	<u>1975</u>	<u>1976</u>	<u>1977</u>	<u>1978</u>
Bahrain	90.2	279.2	203.3	157.1
Egypt	682.7	810.0	982.4	1,134.1
Iraq	309.7	381.8	210.9	316.6
Jordan	195.4	234.0	301.8	235.0
Kuwait	366.1	471.5	547.8	744.8
Lebanon	402.3	48.5	123.8	142.8
Libya	231.5	276.6	313.7	425.0
Oman	74.7	57.1	56.9	65.1
Qatar	50.3	78.7	113.1	76.7
Saudi Arabia	1,501.8	2,744.1	3,575.3	4,370.1
Syria	127.8	272.2	133.6	142.5
United Arab Emirates	371.5	424.8	515.1	493.2
Yemen Arab Republic	8.3	25.4	46.4	30.6
Yemen P.D.R.	2.8	4.4	30.9	25.9
TOTAL U.S. EXPORTS	4,417.1	6,138.6	7,154.9	8,359.5
Increase over previous year	--	13.9%	16.6%	16.8%

Source: U.S. Department of Commerce

TABLE 2. Share of Arab Market Held by Major Western European and North American Exporting Countries, 1973-77

	1973	1974	1975	1976	1977
Percent of Market:					
France	28.7	25.1	23.7	20.1	19.8
United States	22.2	23.1	23.9	27.1	26.2
West Germany	17.0	19.3	20.2	22.1	22.0
Italy	15.5	17.0	16.8	15.2	15.3
United Kingdom	15.3	12.8	13.9	14.0	14.9
Canada	1.3	2.1	1.5	1.5	1.8

Source: Petroeconomic File, July, 1978, based on IMF Data

industry. But according to official government figures, growth in 1977 and most of 1978 was only about 2.5 percent, and the construction industry stagnated.

Exports have paid for only about 51 percent of Syrian imports in recent years; Arab aid has paid for 43 percent. The country's 1976 balance of payments deficit sharply reduced its capacity to import, but by the end of 1977, Arab aid was restored and her economic outlook began to improve, raising American exports to Syria in the second half of 1978 50 percent higher than in the first. A new current account deficit in 1978, however, will in all likelihood restrict Syrian imports once more.

Our exports to Iraq amounted to \$316.6 million in 1978, 50 percent higher than the \$210.9 million for 1977. Because the Iraqi Government severed diplomatic relations with the U.S. in 1973 and has not resumed them, the drop in U.S. exports to Iraq in recent years was widely interpreted as a response to anti-boycott legislation. But the 1978 increase indicates there are other factors at work. Some Commerce Department trade specialists believe Iraq "has undertaken a major review of its commercial relations," and is directing more of its purchases to nations which buy large amounts of its crude oil. In addition, relations with the Soviet Union have cooled to some extent. The 1978 trade figures suggest that these factors may be at least as important to Iraq's import policies as U.S. anti-boycott laws.

Aside from the most militant Arab states cited above, the U.S. has continued to do extensive business with the three Arab countries which represent the largest Arab export markets for the U.S. -- Saudi Arabia, Kuwait, and Egypt. Collectively, they have increased their purchase of U.S. goods by two and a half times since 1975, and each country has set a new high each year.

Even Lebanon, whose economy was brought virtually to a standstill during the 1975-1976 civil war, and whose purchases from the U.S. plunged to \$48.5 million in 1976, raised its U.S. imports to \$124 million in 1977, and doubled that rate during the first five months of 1978. The political situation worsened in the second half of 1978, and the Commerce Department noted that the "security situation was now so poor that business travel to Lebanon is no longer advised." Nevertheless, U.S. sold to Lebanon \$142.8 million worth of goods and services in 1978, a 15 percent increase over the previous year.

Trade figures for some Arab countries have seesawed because of sizable one-time payments for major projects, capital goods or aircraft. Jordan's imports from the U.S. rose sharply in 1977, for example, when she took delivery of two Boeing 747s (88 million), and Bahrain import figures were swelled by \$91 million worth of U.S. aircraft in the same year.

The volume of American exports is also affected by limitations on expenditures set by several Arab countries. After the 1973 oil-price rise, the Arab oil states seemed to have more money than they could ever spend; but more recently, as oil markets have been glutted and the cost of goods and services from the industrial countries has risen, several oil-producing states have had to constrain their spending. In addition, the more sparsely populated Arab countries are approaching the limits of development that they can either use or manage. Thus, Qatar's 1978 budget reportedly allocated \$1.3 billion for development, an 18 percent drop from 1977. (An annual inflation of approximately 25 percent imposes a further real limit on expenditures.) An economic slowdown in the United Arab Emirates in 1977 forced a measure of buying restraint there; Oman is curtailing its spending because it worries about dwindling oil reserves; and Bahrain, too, authorized no new major projects for 1978 and 1979.

Indeed, in 1978, the only Arab nations running current account surpluses were Saudi Arabia, Kuwait, and the United Arab Emirates.

Problems in U.S. Exporting

Though internal economic and political problems inhibit Arab purchases to some degree, the U.S. has benefitted from a rapid expansion of U.S. trade with the Middle East, precisely at a time when it is experiencing increasing trading difficulties in other parts of the world. America's record trade deficit of \$28.45 billion in 1978 exceeded the earlier record of \$26.7 billion for 1977, and a Department of Commerce analysis of U.S. trade with 33 nations indicates that our market share of imports has declined in more than half of those countries since mid-1977.

The U.S. percentage of manufactured goods and chemicals exported by the 15 major industrial nations has been falling for a number of years. It was 30 percent in the late 1950's as against 21.1 percent in 1975, 20.5 percent in 1976, 19.8 percent in 1977, and 18.9 percent in the first quarter of 1978.

Along with this relative decline in exports of our manufactured goods, there has been an erosion of the U.S. position in the international construction and construction equipment industries -- which represent sizable portions of imports by Arab countries, where the development of infra-structures has been a major priority.

A study by New York consultants William Reinhardt and Nancy Hall has found that of the 542 major construction contracts -- valued at \$86.4 billion -- awarded by 14 Middle Eastern countries between June 1975 and April 1978, 51 percent

of the dollar value went to European firms, 27 percent to Asian contractors, and only 10.3 percent to U.S.-based companies. Measured by the number of contracts received, the U.S. share was only 9.8 percent.

American contractors have been among the businesses that warn the most vigorously about the disastrous effects of anti-boycott legislation on their competitive position; but it is now clear that the problems encountered by U.S. construction firms not only preceded the anti-boycott legislation, but had other, far more deeply-rooted origins. According to the Reinhardt and Hall figures, U.S. contractors won (in dollar value) 5.6 percent of Middle East construction contracts in the June-December, 1975 period, 11 percent in 1976, 12.6 percent in 1977, and 11.3 percent in the first quarter of 1978.

After years of undisputed global leadership in heavy construction, this country has slipped to fourth place, according to the National Constructors Association, a Washington-based trade association. U.S. construction companies operating abroad now rank behind West Germany, Italy and Japan, and are being challenged by South Korea and Great Britain. Paul Gibson, in an article entitled "Another Domino is Falling" in the December 25, 1978 issue of Forbes, wrote that this country's high wage levels were not the biggest problem because U.S. firms generally subcontract their labor-intensive work. Nor is the problem technology, for the U.S. is still widely recognized as a leader. Nor is it anti-boycott legislation. Rather, Gibson said,

the biggest threat is the willingness of foreign nations to subsidize the work of their construction firms while U.S. construction firms must operate under free enterprise rules.

In the first massive wave of Middle East construction, from 1974 to 1976, most contracts were let on a cost-plus management-fee basis. But after major cost overruns, several Arab countries began to insist that general contractors complete their projects for prearranged sums. However, having been badly burned by inflation and currency fluctuations, many U.S. construction firms flatly refuse to quote fixed-prices for contracts abroad. But, Forbes noted:

In sharp contrast, foreign firms are willing to work on fixed-price contracts because their governments, in one way or another, protect them against losses. Italy and Korea are among the worst offenders in this respect. This protection ranges from generous tax breaks and outright tax holidays to what U.S. executives claim, but cannot prove, are government

guarantees against any corporate losses on fixed-sum contracts. For U.S. firms no such aid or breaks are available.

In most international construction projects today, the contractor's home country government's export financing agency extends credit to the foreign buyer. (In the U.S. this is done by the Export-Import Bank, in France by COFACE, and by Hermes in West Germany.) Under international agreement, these agencies are supposed to extend credit at the same or similar rates of interest although, Forbes pointed out:

What often happens in practice is that governments eager for work will set about circumventing that agreement. The easiest way is to announce a grant-in-aid for, say \$250 million at a 4% interest rate, to the country letting the construction award. The U.S. rarely allows such grants for industrial projects.

U.S. firms operate abroad under an additional handicap. A successful bidder must post performance guarantees or letters of credit which can amount to over 30 percent of the contract and may entail many millions of dollars for large projects. But our banking laws sharply circumscribe the amounts that can be lent to American construction firms, most of which have limited capitalization. By contrast, as Business Week reported on September 18, 1978, West German banks hold large, often even controlling interests in the nation's five largest construction firms. Thus, not only do these firms have greater access to credit than American companies, but they enjoy the protection of West Germany's Federally-sponsored insurance against contract cancellation.

Similarly, in mid-1978 a syndicate of major American banks, led by Citicorp, was eager to arrange a \$300 million performance guarantee to the Hyundai Construction Company for a Middle East contract, because this loan was fully guaranteed by an arm of the South Korean Government.

Such government backing has been especially important in the dramatic rise of Asian, and particularly South Korean, construction activity in the Middle East. South Korean firms did not arrive there until 1972, and did not land their first substantial contract until 1976. After that, according to Forbes, "of the last 19 jobs let by the U.S. Corps of Engineers in Saudi Arabia, the Koreans took 11, the U.S. only 4. For every \$1 of work awarded to U.S. firms, the Koreans garnered \$3." Although South Korean contractors are thought to be losing money on many construction jobs, an article in the May 29, 1978 Business Week, "Korean Contractors Invade the Mideast," revealed that:

Seoul is pushing foreign construction work to offset the country's spiraling cost of imported oil -- \$1.7 billion last year. To encourage Korean contractors, Seoul provides them with low-cost loans, loan guarantees, and five-year tax exemptions on exported construction material and equipment.

This vigorous, often subsidized, competition has had an impact on U.S. sales of construction-related equipment. Our exports of such products increased five-fold between 1967 and 1975, but in the past three years U.S. sales -- except for replacement parts -- have hovered around \$2.5 billion and may actually have dropped in real terms. The problem of U.S. manufacturers, as one construction expert put it to Forbes, is that: "If you're a Korean contractor laying a pipeline, you're sure as hell not going to order pipe from Pittsburgh." In other words, said Forbes:

Given a choice, a construction engineer orders from his own country. He knows the product and trusts the supplier. And too clearly the figures bear this out.

In sum, American primacy in international construction has been challenged, U.S. exports of construction-related equipment have been stalled, while Korean exports of these goods have soared from \$275 million in 1970 to the current \$2 billion a year.

American exporters have been saddled with other problems. Relatively low productivity in some fields of American manufacture makes U.S. export goods more expensive despite the continuing weakness of the dollar -- which normally would make them cheaper; and there are questions about how willing and able American firms have been to mount the kind of continuing sales campaigns necessary for success in the Middle East. Then there are our anti-bribery laws, as well as taxes on earnings outside the country.

Yet, despite these handicaps, the bottom line remains a continuing dramatic rise in U.S. exports to the Arab world, a record that obliges opponents of anti-boycott legislation to search out occasional examples of lost sales, and to speculate on what might have been without these regulations. In the complex, close-mouthed world of international trade, it is often hard to determine why a sale was lost, or even that it was "lost." Therefore, to argue about what might have occurred under different circumstances cannot be anything but pure speculation -- which, in economic analysis as well as in the marketplace, is a decidedly risky undertaking.

Adjustments in the Boycott

There is strong evidence that the major impact of U.S. anti-boycott legislation has been not on our exports to the Middle East, but rather on the Arab countries' boycott itself. In occasional formal pronouncements, and more frequently in practice, the Arab states have drawn back from some of their more extreme demands and moved toward compliance with U.S. law.

An article in the April 1978 American Banker, entitled "U.S. Boycott Laws Seen Not Affecting Trade with Arabs," quoted a New York banker who had originally feared "the Arabs were not going to budge." Now, he said, "we've seen a lot of modification on the part of the Arabs." And, according to the Houston Business Journal of May 29, 1978,

Margaret Martin, an attorney with Kurth, Andrews, Campbell and Jones, said companies here are reporting more success in getting Arabs to reword documents so as not to violate U.S. laws. She said businessmen have indicated success even in Libya, which is regarded as one of the most adamant of Arab nations.

Similarly, at a July 14, 1978 conference in New York sponsored by the American Management Association, experts on Middle East trade said that except in Libya, Iraq, and Oman, negative certificates -- statements that goods are not of Israeli origin -- had given way to positive certification that the goods sold are made in the U.S. And one speaker reported that several firms had shipped even to Libya without negative certifications.

Then, in his September 1978 speech in Chicago, Stanley J. Marcuss said negative certificates of origin were "fast becoming a thing of the past." Moreover, he pointed out that in the spring of 1978 Saudi Arabia had stopped demanding certification that vessels and insurers were not on the Arab League blacklist. The Saudis now accept statements of general commercial eligibility which contain no boycott-related terms. And more recently, they also dropped the demand that powers of attorney containing boycott provisions must be included in registrations of patents and trademarks.

In August 1978 Kuwait, followed by almost all boycotting countries, deleted from government contracts the clauses calling for a company's specific compliance with boycott regulations and substituted one that says the American firm generally agrees to comply with the host country's laws. Instead of requiring that American subcontractors employ no blacklisted suppliers or subcontractors, as happened in the last, many Arab government contracts now reserve the right to select specific suppliers or

subcontractors unilaterally, which is acceptable under U.S. law.

In the past, letters of credit were a particularly troublesome problem, because they, too, often required negative certificates of origin and contained other boycott stipulations; but again, Arab states have made important changes to adjust to U.S. laws. For example, Abu Dhabi and Bahrain have simply deleted the boycott references; since April 1978 Kuwait has been accepting positive certificates of origin, as has Qatar, which also deleted the ban on buying insurance from blacklisted companies. Saudi Arabia, too, has made these and other changes in shipping and insurance documentation to accommodate U.S. vendors.

These changing attitudes and practices seem to have been confirmed by a Department of Commerce report of a recent decline in the number of boycott-related requests filed there according to the Export Administration Act.

But Egypt, of course, has made the most dramatic moves. The Peace Treaty signed by President Anwar el Sadat and Prime Minister Menachem Begin provides for removal of all boycotts of each nation by the other. More, a dispatch from the Arab Press Service International Edition, dated October 16, 1978, said:

Last year, when President Sadat began his dialogue with Premier Begin, he also let it be known in high economic and diplomatic circles that Egypt was prepared to start negotiations with major companies blacklisted by the Boycott Office. Discreet talks began in Cairo with companies like Colgate-Palmolive, Motorola, Cadbury-Schweppes, as well as giants like Ford, Coca Cola and Xerox.

These negotiations led to what the November 1978 bulletin of the Arab-American Association for Commerce and Industry called "a new interpretation to the pan-Arab boycott." According to this bulletin, the Egyptian Government's position is that a boycotted company can "atone" for dealings with Israel by investing more heavily in Egypt. Consequently, the Coca Cola Company began to negotiate its return to the Egyptian market after an absence of more than 11 years, and the long-boycotted Xerox Corporation is open for business in Cairo. True, Egypt has formulated some of the new regulations to keep them in technical compliance with the Arab League boycott, but the fact remains that it has unilaterally been doing business with blacklisted firms if their investments in the Arab world equal or outweigh their dealings with Israel.

The Arab Press Service contends that this development "heralds the impending collapse of the Arab economic boycott of Israel." Indeed, the October 16, 1978 dispatch cites a question

by a leading Arab economist: "After Egypt (the most populous Arab country) has opened its doors to blacklisted companies, how can the rest of the Arab world maintain an effective boycott?" Indeed, the dispatch concludes: "The Arabs' boycott weapon against Israel is crumbling. Once Egypt has broken the boycott, then, within a year, more than half the population of the Arab world will join in."

These observations may well prove premature and too optimistic for believers in free trade. Nevertheless, they show how easily Egypt could back away from the boycott principles. In fact, the boycott has always been more impressive by ideological than by economic standards, and has frequently been breached by some Arab countries for reasons of self-interest. Those who do so include not only such moderate regimes as Jordan's, which actually carries on a small trade with Israel across the Jordan River, but such militant regimes as Libya's, whose purchases from the U.S. keep soaring.

Thus it is not surprising that a strong American stand on the secondary and tertiary boycotts has not slowed the growth of U.S. sales to the Arab countries, but, on the contrary, led Arab states to adjust to U.S. boycott law. Undoubtedly, an occasional sale has been lost, but considering this country's worldwide difficulties as an exporter, many other nations would envy its sales record in the Arab states.

In 1978, Juanita Kreps stated that "if we insist -- while respecting the sovereignty of other nations -- on the right to protect our own, if we insist that business without principle is business not worth having, then we will be successful." The record so far strongly suggests she was right. The U.S. has, in fact, acquired an important share of the Arab world's market for imports, and we have done so while adhering to our traditional commitment to free markets and to the freedom of men and women.

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