

Israel-Egypt: Economic Benefits of Peace

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Any gains from a peace settlement would depend upon a substantial change in the siege mentality in both Israel and Egypt to a more optimistic view of the future. The short-run benefits of such an atmospheric change would be tangible -- though not dramatic -- and could include a reduction in the defense burden and a shift of resources into the civilian economy. The potential for such a dividend is greatest in Israel, which since the 1973 war has put more of its eggs into the military basket than has Egypt. Other major benefits -- such as national as well as regional development programs -- would take much longer and would hinge on the ability of both countries to obtain Arab and Western financing.

Israel

1. Considerable potential for an economic peace bonus exists in Israel, depending on Tel Aviv's actions. Most importantly, a peace settlement would ease the manpower constraint on Israeli growth, facilitating increased industrial output and exports. If, for instance, Tel Aviv decided to demobilize the 50,000 additional troops in place since 1972 (20,000 in 1979 and 30,000 in 1980) and to divert the cost of maintaining these troops into civilian investment and tax breaks, we estimate that GNP could grow an additional half percentage point next year and an additional one percentage point the following year. Since a peace settlement probably would attract new immigrants, reduce the number of Israelis seeking employment abroad and facilitate labor inflows from Arab countries, the overall improvement in the manpower situation would likely whittle a few percentage points from Israel's expected annual inflation rate of 40 percent plus.

2. The alleviation of political risk associated with a peace settlement holds further potential for GNP gains -- possibly as much as one percentage point in 1979-80 -- since foreign investment and tourism would be higher than they would be if tensions remained at present levels.

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- Assuming the Arab boycott were lifted, the highly skilled manpower pool in Israel should attract increased foreign investment in re-export industries such as electronics and in research and development companies.
- Already a major industry, tourism would benefit since the Holy Land holds great attractions for Christian, Jews, and Muslims alike. Increased construction of hotels and other tourist facilities would boost Israeli demand while tourist expenditures would help cover some of the foreign exchange costs of accelerated growth.

3. Finally, although full potential would only develop over time, Israel could increase its share of Arab markets. Israel already produces many goods that the Arabs currently buy in the West, including processed foods, communications equipment, scientific and medical equipment, pharmaceuticals, and furniture. Israeli economists estimate that Israel could export \$100 million annually to Egypt alone -- about 3 percent of current total exports.

Egypt

4. Peace would allow Egypt to concentrate on economic development and the task of transforming its inefficient, centralized economy into the more dynamic, mixed economy envisaged by President Sadat. While a settlement would not immediately translate into large economic gains, it would speed up changes that would yield substantial benefits over the medium term. Most importantly, peace would encourage: (a) more rapid foreign exploration and development of promising oil potential in the Gulf of Suez, (b) increased foreign and domestic private investment, and (c) continued rapid growth in tourism.

5. Eventually Cairo might be able to tap Israeli expertise in desert agriculture to help achieve the long-held Egyptian dream of turning wasteland into farmland. Israel's need for petroleum, natural gas, and other raw materials will provide a close ready market for Cairo, and Tel Aviv might be willing to help in developing Egypt's raw material resources.

6. Direct benefits on the military side are likely to be much smaller than in Israel. Cairo is spending relatively little of its own money on defense, and any force reductions are likely to be of unskilled soldiers, doing little to ease Egyptian manpower shortages of skilled workers and managers. Peace, moreover, entails some dangers for Cairo:

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- Economic expectations long held in check by the state of hostilities could accelerate beyond real short-run gains.
- Generous aid flows from Saudi Arabia and other conservative Gulf states might be reduced; for example, these countries might divert some aid to help a Palestinian entity if one were established.

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