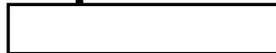


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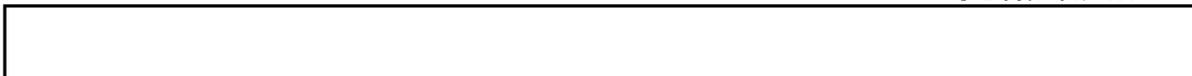
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State Dept. review  
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DIA review(s) completed.

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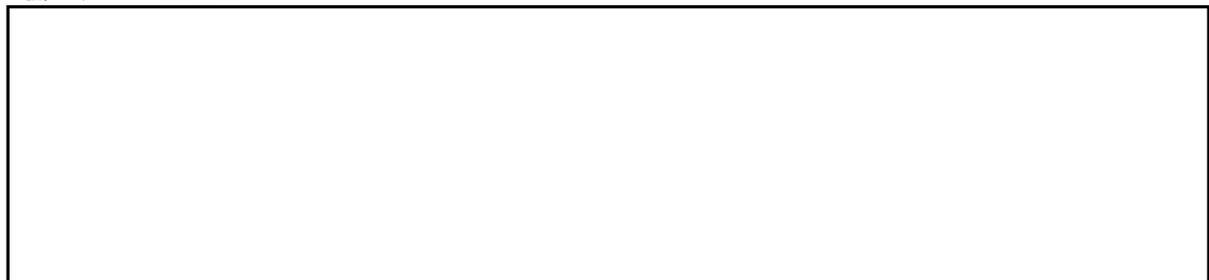
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ARAB STATES - ISRAEL

Prime Minister Rabin's outline of Israel's negotiating strategy, laid out in a press interview on Tuesday, could push the Arabs into a more intransigent position.

Rabin offered Egypt a virtually immediate agreement on a second-stage withdrawal in the Sinai Peninsula, untied to explicit political commitments from Cairo other than a prolonged extension of the cease-fire. His offer, however, is woven into an overall strategy designed to delay for years the conclusion of a comprehensive peace settlement. As outlined, Rabin's plan also seems intended to keep Egypt quiescent and unprepared for a war fought either on its own front or in coordination with Syria.

Rabin prefaced his offer of a Sinai disengagement with a clear statement of Israel's intent to play for time. Israel is now powerless to change international realities, he said, and might need as long as seven years before the West is free from dependence on Arab oil. The implication is that negotiations for an overall settlement at this later stage would find Israel better able to withstand pressures to make concessions.

Rabin spoke of a Sinai disengagement agreement in terms of how it would facilitate Israel's delaying strategy. Such an agreement, he said, would keep Egypt out of the Soviet orbit and thus, by implication, out of war. He said that Israel has six weeks in which to decide how to handle Egypt--a reference to the scheduled visit of Soviet party chief Brezhnev to Cairo in mid-January.

Rabin noted indirectly that another withdrawal would help Egypt's unpreparedness, implying that the disengagement agreement last January resulted in the cessation of Soviet arms deliveries to Egypt and thus the limitation of Egypt's military capabilities. He stated that if Israel then had to fight a war with Syria, Egypt would be reluctant to join and Israel would be in a "more comfortable position."

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The Egyptians have not reacted officially to the interview, beyond dismissing it as intended primarily for internal Israeli consumption. Rabin's remarks are potentially embarrassing to President Sadat and could frustrate his desire to proceed with a further agreement in the Sinai.

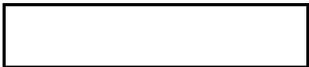
Egyptian agreement to disengage on Rabin's terms would signify, in Arab minds, Sadat's acquiescence in Israel's strategy to put off concessions to the other Arabs for years. This would magnify Arab suspicions that Egypt is interested only in regaining its own territory. Sadat would be seen, moreover, to be acquiescing in the waiting game on terms that would exploit Egypt's own present military weakness as well as weaken overall Arab political and military strength.

Syria's government-controlled press has interpreted Rabin's statement as further evidence of Israel's attempt to isolate Damascus from the negotiating process and to "paralyze" efforts to reconvene the Geneva conference. Rabin said nothing about negotiations with Syria, mentioning Damascus only in connection with possible renewed warfare.

In unusually sharp attacks, two Syrian newspapers yesterday, citing Rabin's interview, accused the US of backing Israel's aims and attempting to divide the Arabs by putting forth schemes for partial agreements that exclude Syria and hinder achievement of a comprehensive peace.

Damascus is deeply suspicious that Egypt intends unilaterally to negotiate a final Sinai settlement. Rabin's proposal will reinforce these suspicions, whether or not Egypt agrees. Rabin's remarks are likely to generate intensified Syrian demands for resumption of talks in Geneva.

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SOUTH KOREA

Political tensions in South Korea have eased considerably since President Ford's visit, and the Pak government seems willing to tolerate opposition activity so long as it does not spill over into large-scale demonstrations.

Antigovernment protests have fallen off across the board. This results in part from general fatigue in opposition ranks. In addition, opposition leader Kim Yong-sam has been restrained by dissension within his New Democratic Party, and he sees a better chance for taking on the government later in the winter, when the country's economic difficulties are expected to mount.

Meanwhile, a "united front" of influential religious, media, and political leaders--including Kim Yong-sam--intends to keep the main opposition issues alive, especially demands for constitutional revision and the release of political prisoners.

The government's more restrained tactics have also contributed to the relative calm, although the regime has been active behind the scenes in regaining the political initiative. In the National Assembly, threats and bribes have been used to encourage challenges to Kim Yong-sam's leadership.

Prime Minister Kim Chong-pil reportedly told National Assembly leaders recently that the government is considering some concessions, but only if an "appropriate" political climate could first be established in Seoul. In view of the deep differences between government and opposition, however, it is doubtful that the present lull can be turned into a durable political accommodation.

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UNITED KINGDOM

At the annual Labor Party conference last week, left-wing Laborites pushed through resolutions attempting to limit the government's flexibility on a number of foreign policy issues, particularly the EC membership question. Despite this demonstration of left-wing strength, moderates led by Prime Minister Wilson generally held their own. The balance of power between militants and moderates seems essentially unchanged.

The conference overwhelmingly approved a decision in October by the party's extra-parliamentary organization, the National Executive Committee, to censure the government for authorizing joint naval exercises with the South African navy. The delegates demanded implementation of a resolution passed at the conference last year urging termination of military relations with South Africa. After the censure in October, however, government officials promised to re-examine the merits of the Simonstown Pact, the agreement providing for the recent naval maneuvers.

As expected, the conference was the forum for strong anti-EC sentiment. Apparently fearful that Wilson or Foreign Secretary Callaghan might campaign for a "yes" vote in the coming referendum on EC membership, the delegates unanimously demanded assurances that the government would present both sides of the membership issue. A second, more controversial resolution, passed by a slim margin, called for "safeguards" before the government accepts new conditions for continued membership. The delegates also demanded that a special party convention be held before the referendum. All these measures are designed to compel the government to reject the results of renegotiation, but Labor governments historically refuse to consider themselves bound by conference or rank-and-file votes unless passed by heavy majorities.

Pro-marketeters received encouragement from party elections last week, when moderates held on to several important posts. Cabinet member Shirley Williams and trade union leader Tom Bradley, both strong supporters

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of EC membership, were re-elected to their posts in the National Executive Committee despite strong opposition from the left. One committee seat, however, was taken over by a militant. The Parliamentary Labor Party, the influential organization of backbench Laborites, elected four moderates and only two militants to the organization's committee responsible for liaison with the government.

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ITALY

Aldo Moro's center-left government--composed of Christian Democrats and Republicans, supported in parliament by the Socialists and Social Democrats--faces its first test today in a vote of confidence in the Italian Senate; the Chamber of Deputies will vote over the weekend or early next week. Moro will probably get parliament's endorsement, but strains have already begun to appear in his new administration.

The swearing-in of Moro's cabinet on November 23 did not put an end to the bickering that fueled the seven-week-long political crisis. The Socialists, in particular, have criticized the composition of the cabinet, interpreting certain changes as concessions to right-wing elements. The Social Democrats, whose long-running feud with the Socialists was the centerpiece of the recent battle, countered with the charge that the Socialists were backing away from their commitment to support Moro.

All of this had led a left-wing Christian Democratic leader to remark publicly that Moro's government will not last long. Moro himself has labeled his administration "transitional." In a speech this week, he made it clear that his main goal is to eventually bring all four parties back together in another center-left coalition.

Judging from the new government's economic program, that will not be easy. The program repeats all of the economic goals of the Rumor government--fighting inflation, redressing the balance of payments, developing the South, maintaining employment--without saying how the parties will resolve their long-standing differences over how to attain them.

Although the Communists are keeping the Christian Democrats under fire for failing to put together a stronger government, they seem inclined to give Moro a breathing spell. For his part, Moro's Senate remarks on the Communists were conciliatory in tone, if not in substance. While reiterating the Christian Democrats'

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intention to maintain a firm distinction between government and opposition, Moro said, as have other center-left prime ministers, that he would "attentively" consider their suggestions on national policy.

A cooperative attitude on the part of the Communists--similar to the "soft opposition" they gave the Rumor government--would be useful to Moro in dealing with one of his most urgent initial problems: defusing the labor unrest that has continued to build up while Italy has been without a government. The unions yesterday called their third nationwide general strike in two months in support of higher pay and benefits. Moro is committed to a more intensive dialogue with labor, but he will not be able to accept many of their demands without compromising the four-month-old austerity program.

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SAUDI ARABIA

The appointment of Abd al-Aziz ibn Zayd al-Qurayshi as governor of the Saudi Arabian Monetary Agency reinforces earlier expectations that Saudi investment policy will become more liberal. He is a close friend of the minister of state for finance and national economy, Aba al-Khayl, who favors a shift from the ultraconservative investment practices of Qurayshi's predecessor, the late Anwar Ali.

Foreign officials in Jidda see the selection of Qurayshi as an attempt by Aba al-Khayl and the minister of finance and national economy, Prince Musaid, to assert greater authority over Saudi investment. While Anwar Ali headed the monetary agency, these two officials had little to say in how surplus oil revenues were invested.

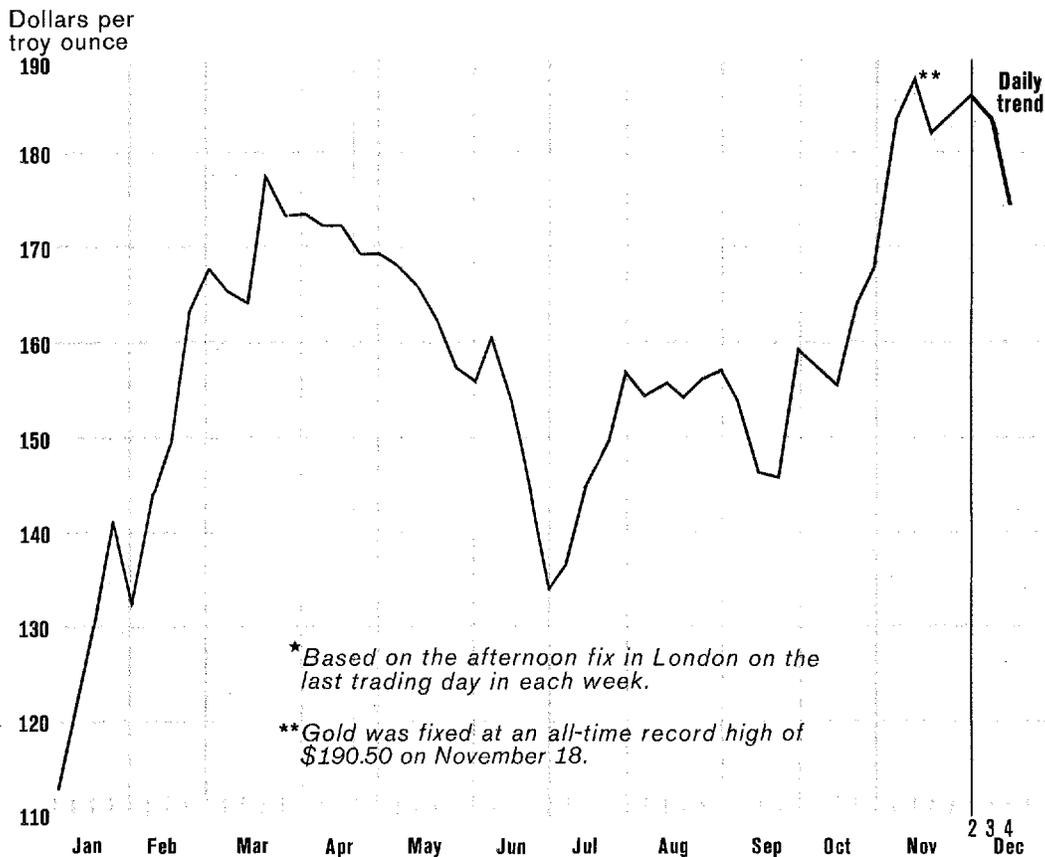
The agency's future role is still in question, however. Besides Prince Musaid and Aba al-Khayl, other leaders such as Prince Fahd--King Faysal's likely successor--and central planning chief Hisham Nazir are also seeking more influence over Saudi investment activities. The idea of splitting the Saudi Arabian monetary agency into a central bank and an investment institution is receiving serious consideration. Other organizations that have been proposed to oversee foreign investment and economic development also might reduce the agency's power.

Qurayshi, educated in the US, is one of a growing number of young, Western-oriented commoners who have moved into important government positions in recent years. About 40 years old, he has little experience in international finance and will probably rely heavily on the advice of Aba al-Khayl. Qurayshi's primary interest has been in domestic economic development. A friend of the US, Qurayshi has been active in recent US-Saudi discussions on economic cooperation, particularly on manpower training needs.

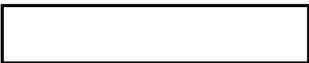
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INTERNATIONAL MONETARY DEVELOPMENTS

Gold prices are falling worldwide in the wake of the announcement that the US will auction 2 million ounces on January 6. Shortly after the announcement on Tuesday, heavy sales drove prices down more than \$6 in London to \$178 per ounce. Yesterday the slide continued, with the closing bid at \$174, the lowest in a month.

The price of gold increased from \$116.50 at the beginning of the year to a high of \$190.50 on November 18. Part of the reason for this has been the anticipated demand in the US following the end of restrictions on private ownership of gold after the end of the year. The coming auction and Secretary Simon's statement that additional government sales may be forthcoming should tend to deflate gold prices.

The 2 million ounces are less than 1 percent of US gold holdings, and between 5 and 10 percent of the new gold that has entered the market so far this year. Gold traders are concerned that this amount will have a depressing effect on prices because it considerably exceeds the volume traded on an average day.

Initial foreign reaction to Washington's decision has been slight. The South African finance minister sees no need to change his government's marketing policies. He did leave open the possibility of withholding South African gold from the market, should the price decline appreciably. Governor Sasaki of the Bank of Japan predicted that the US action would have little effect on the price and commented that the move was taken to prevent a sharp rise in the price which might have been interpreted as a weakening of the US dollar.

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JAPAN

The Japanese Defense Agency budget request for fiscal year 1975 shows a 25-percent increase over 1974,

Although the figure is designed only to keep pace with Japan's skyrocketing inflation and follows guidelines set by the Ministry of Finance, defense officials apparently doubt that the full amount will be provided. The military received about \$3.6 billion in 1974, which is under 1 percent of Japan's gross national product.

Several of Japan's defense procurement programs are already being delayed in anticipation of budget cuts. Programs affected include fighter and ground-support aircraft development and armor and destroyer production.

Japan has been hit hard by the rise in the price of oil and other raw materials; labor costs have also shot up. Japan's military forces are expected to absorb their share of the economic burden, with the result that military modernization will probably be set back several years.

The Finance Ministry is expected to announce the figures for 1975 late this month or in early January. Although the budget is subject to the approval of the cabinet and the Diet, this is usually only a formality.

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CHINA

Business transacted at the recently concluded fall Canton Fair was at its lowest level in years. The value of contracts signed--about \$700 million--dropped about 30 percent below the level of the spring fair and about 45 percent below the fair last fall. The number of traders in attendance fell by about 10 percent from last spring.

Chinese purchases at the fair declined sharply. Peking has been postponing or cutting back imports of farm products and some industrial materials in the face of a rising trade deficit and a temporary shortage of foreign exchange. China also has been shifting much of its purchasing outside the Canton Fairs.

Sales of China's traditional exports suffered from the depressed state of the world economy. Businessmen arrived in Canton with little interest in adding to large inventories of Chinese goods purchased at high prices at previous fairs. Although Chinese prices were generally lower than at the spring fair, they often remained sufficiently above the level of world prices to preclude business.

The dismal performance of Chinese sales will retard export growth next year. Increased petroleum sales will probably offset the decline in traditional exports, but the sharp increase in export earnings achieved in 1973 and 1974 is not likely to be sustained. Peking will probably continue to restrict less essential imports and may widen the use of credits in the year ahead.



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SOUTH VIETNAM

Heavy fighting remains concentrated in the northern provinces of South Vietnam. Government troops reportedly have made little progress against Communist forces on high-ground positions south of Hue, and resistance also has stiffened against South Vietnamese attempts to recapture lost territory in the lowlands farther south. There also are reports that activity has picked up in Pleiku and Binh Dinh provinces.

There continue to be indications that the Communists are reorganizing and streamlining some of their forces in the southern half of the country. The 75th Artillery Command's three regiments reportedly have been assigned the mission of providing direct support to each of the Communists' three main force divisions. Such a reorganization would improve artillery support for these units.

In the delta, a recently captured document indicates that a new Communist division may have been formed from existing units. If confirmed, this new division would improve command and control over Communist infantry forces now operating in the southernmost provinces.

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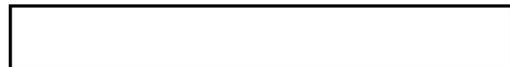


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