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7 June 1965

OCI No. 1771/65
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INTELLIGENCE MEMORANDUM

**BRITAIN'S GOVERNMENT EXPENDITURES
EAST OF SUEZ**

**APPROVED FOR RELEASE
DATE: DEC 2000**

DIRECTORATE OF INTELLIGENCE

Office of Current Intelligence
Office of Research and Reports

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CENTRAL INTELLIGENCE AGENCY
Office of Current Intelligence
Office of Research and Reports
7 June 1965

INTELLIGENCE MEMORANDUM

Britain's Government Expenditures
East of Suez

Summary

One of Britain's main concerns about its overseas commitments is the cost of the "long thin line" beyond Suez. Actual cost figures broken down by geographic area are hard to come by, but our calculations indicate a burden east of Suez of more than a billion dollars annually.

An expense of this magnitude does not represent an extraordinarily high percentage of British GNP (a little more than one percent), but in their current hours of financial strain, the British feel they have to examine all the straws on the camel's back. There is moreover the consideration that the cost includes sizable expenditures which Britain wants especially to minimize because they enter into the balance of payments. We estimate that the adverse effect on the balance of payments may be as high as 350 million dollars a year.

This amount is less than the income, nearly half a billion dollars, earned annually by Britain from investments east of Suez. However, many Britons feel that this income should not be considered an economic justification for the costs. Their opinion is that the income would by and large still flow to Britain even if drastic economies were made in expenditures. The possible saving of some hundred millions in the balance of payments is large enough to engage the grim attention of a government anxious to restore international confidence in the pound.

Calculation of Costs

1. A recent article in the Daily Telegraph (Conservative) expressed a growing viewpoint: "We

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must disengage east of Suez in order to engage the better in Europe. Where we cannot do so, responsibility should be shared..."



2. Although the British have not provided any real accounting of these costs, some indication of the economic burden is available from occasional figures thrown out in parliament and other forums. (See Annex 1) We have attempted a costing calculation of our own as an independent check on these figures. (See Annex 2) Our calculation suggests an expenditure of around 900 million dollars a year to maintain British forces east of Suez.

3. We caution that this figure (amounting currently to 18 percent of overall defense expenditures) is an approximation, indicating only the order of magnitude. We stress further that our estimate does not represent the saving that would be realized if all the forces east of Suez were withdrawn; if the forces were still kept in being after withdrawal, they would then still be draining Britain's treasury.

4. Although defense expenditures are much the largest part of Britain's burden, there are also the additional expenses of military assistance payments and other aid to foreign governments. (See Annex 3) Our estimate of these payments by the British treasury over and above the expense of maintaining Britain's own military forces is 240 million dollars. This brings Britain's burden east of Suez to over a billion dollars annually in round numbers.

Balance-of-Payments Impact

5. The burden is supportable under ordinary circumstances by an economy with a GNP of more than 80 billion dollars. The cause for concern is Britain's balance-of-payments deficit. It was a record-breaking 2 billion dollars last year. International apprehensions about sterling devaluation--which might in turn generate a run against the dollar--are widespread. The British authorities now have to support the pound against almost constant speculative pressure. In these circumstances, Britain considers its commitments east of Suez to be

especially onerous insofar as they bear on the balance of payments.

6. British figures are only partially helpful in providing information on this aspect of the problem. The published balance-of-payments accounts give no geographic breakdown that would indicate the impact of expenditures attributable to the area east of Suez specifically. We do, however, have data from which we estimate that military expenditures east of Suez constitute a drain on Britain's balance of payments amounting to possibly 200 million dollars. (See Annex 4)

7. To this figure we have added the amount for military and economic aid, with an adjustment for exports stimulated by such aid. (See Annex 5) Our estimate of the net drain on the balance of payments comes to roughly 350 million dollars. With all due regard for the margin of error, we are still left with a clear impression of serious pressure on Britain's balance of payments; the amount will be perhaps a third of the expected large deficit in 1965.

8. It is of some advantage to Britain that the transactions in this analysis are in large part with other countries of the sterling area. This increases the likelihood that deficits will be financed by a rise in Britain's pound liabilities to other sterling area countries rather than by a loss of monetary reserves. Even so, the effect is a decline in the ratio of reserves to external liabilities, tending further to erode international confidence in the pound and accelerate the flight of funds from Britain.

British Income from East of Suez

9. Not all of the present balance-of-payments drain would be saved by withdrawal of troops to other areas. Even if the troops were all brought home, the government would still incur expenditures for certain imports needed to maintain them. Whatever the saving, it would presumably be balanced against the possible jeopardy to important British investments which yield large incomes. On the basis of data for selected countries, we estimate that about 150 million dollars

in interest, profits, and dividends is earned annually by the British from their investements east of Suez, exclusive of the earnings from the Middle East oil properties. We are a bit more in the dark about the profits from Middle East oil; this statistic is pretty well shrouded in Britain's balance-of-payments accounts. From figures on the oil revenues of Middle East governments, however, we have estimated that the British earn some 300 million dollars a year on their Middle East oil investments. The sum total of nearly half a billion is well above any balance-of-payments saving that could be realized by withdrawal of forces. (See Annex 6)

10. Many Britons argue against balancing these earnings against the drain. American investments in Middle East oil, they point out, exceed British investments, yet Americans are not garrisoning the area. Western Europe is the market for Middle East oil, they reason, and leverage through exploitation of commercial interest rather than through application of military pressure is declared to be the best assurance for Western investments. There are rebuttals to the argument, but it is apparently persuasive enough to have engendered considerable British sentiment for economizing on expenditures east of Suez or, alternatively, getting Britain's allies to assume more of the burden.

ANNEX 1

Statements in Parliament

On total military costs east of Suez

"...the total directly attributable (annual) cost of our forces east of Suez is expected to be about 320 million pounds (896 million dollars) in 1965-66..." (Secretary of State for Defense Denis Healey in the House of Commons, London A-2855, 19 May 1965)

"...these savings...are not on a scale comparable to the operations east of Suez, which cost about 400 million pounds (1.12 billion dollars) a year." (Sir Alec Douglas-Home in the House of Commons, Hansard, 4 March 1965, Column 1547)

On military costs in Malaysia

"It really makes no sense to spend over 100 million pounds (280 million dollars) a year--or, if we include the Far Eastern Royal Navy operating in Singapore, about 225 million pounds (630 million dollars)--to protect British assets in Malaysia..." (Konnie Zilliacus, Labor M.P. in the House of Commons, Hansard, 3 March 1965, Column 1405)

On military costs in Aden

"Is there any need now to keep a base at Aden? ...It costs us between 100 million pounds (280 million dollars) and 200 million pounds (560 million dollars) annually..." (Emlyn Hooson, Liberal M.P. in the House of Commons, Hansard, 4 March 1965, Column 1611)

On Balance-of-Payments Impact

"...cost of our forces east of Suez...including about 100 million pounds (280 million dollars) across the exchanges." (Secretary of State for Defense Denis Healey in the House of Commons, London A-2855, 19 May 1965)

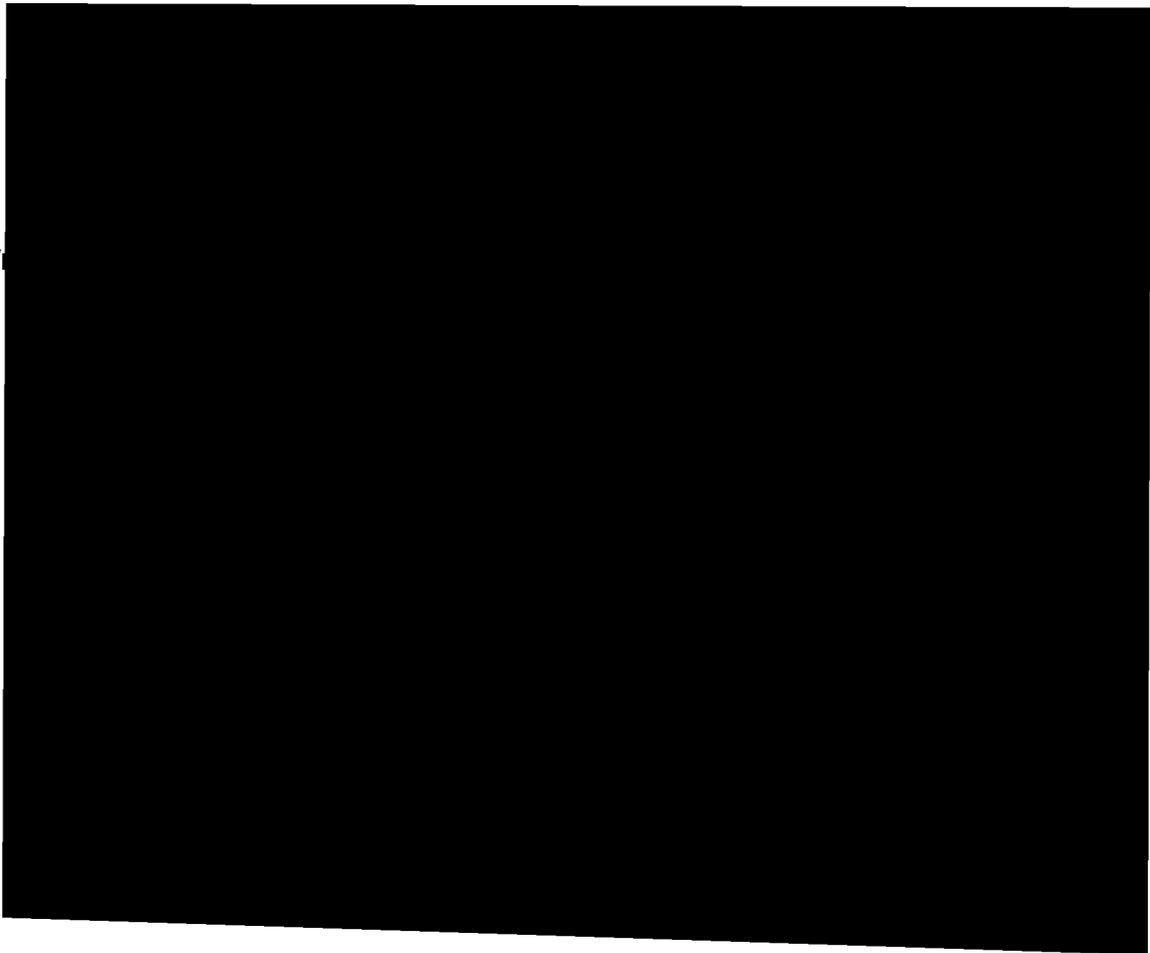
ANNEX 2

Estimated British Military Expenditures East of Suez

(in millions of US dollars)

<u>Service</u>	<u>Amount</u>
Army	460
Navy	240
Air Force	<u>190</u>
<u>Total</u>	<u>890</u>

Explanatory Note



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ANNEX 3

British Aid to Countries East of Suez, 1964

(in millions of US dollars)

<u>Area</u>	<u>Military Aid</u>	<u>Bilateral Economic Aid</u>	<u>Total</u>
Middle East	20	30	50
South Asia	21	126	147
Southeast Asia	<u>29</u>	<u>14</u>	<u>43</u>
<u>Total</u>	<u>70</u>	<u>170</u>	<u>240</u>

Explanatory Note

In calculating the burden on a donar country, there are reasons both for and against differentiating between grants that are cost-free to the recipient country and repayable credits that bear interest. The above tabulation on aid excludes private investments but includes official credits, which are ordinarily extended on terms more generous than the recipient country could obtain in capital markets.

ANNEX 4

Military Expenditures Directly Entering
Into Britain's Balance of Payments

We do not have statistics for British military expenditures abroad in support of forces east of Suez.

Information is available, however, on British military expenditures abroad in 1963 in support of forces based in countries that are not members of NATO. We also have figures for the military expenditures of these countries in Britain. The difference, i.e. the net outflow of funds from Britain resulting from these military expenditures, was 296 million dollars.

On the basis of the ratio of British forces east of Suez to the number in all countries not members of NATO, we would adjust this net outflow figure down to 200 million. We caution that this is a very rough estimate.

ANNEX 5

Balance-of-Payments Impact of Britain's
Commitments East of Suez

(in millions of US dollars)

Military expenditures, net outflow (from Annex 4)	200
Military aid (from Annex 3)	70
Bilateral economic aid (from Annex 3)	<u>170</u>
<u>Subtotal</u>	440
Less exports tied to economic aid	<u>90</u>
<u>Total</u>	<u>350</u>

Explanatory Note

In calculating the balance-of-payments impact, the aid figures should be adjusted to allow for export stimulation from foreign aid disbursements.

The tabulation above already makes an implicit allowance for the effect of military aid on export stimulation; the 200 million dollars for military expenditures, transferred to the tabulation from Annex 4, is net of earnings from military exports.

In the case of economic aid, an explicit adjustment for export stimulation is made on the basis of information that 42 percent of British aid is now wholly tied, that is, requires the recipient government to buy British (See Paris CEDTO 1205, 13 May 1965) Another 16 percent is partly tied. The 90 million figure in the above table is reached by calculating that roughly half the balance-of-payments impact of bilateral economic aid is softened by tying.

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British exports have probably also been encouraged by economic aid which was not tied, but this effect is indeterminate and we have not allowed for it in our calculations.

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ANNEX 6

Britain's Annual Income From
Investments East of Suez

(millions of US dollars)

<u>Area</u>	<u>Gross</u> <u>(Payments to UK)</u>	<u>Net</u> <u>(After Payments from UK)</u>
Selected Countries	193	137
Middle East Countries	<u>325</u>	<u>300</u>
<u>Subtotal</u>	518	437
Other Countries	<u>undetermined</u>	<u>undetermined</u>
<u>Total</u>	<u>550</u>	<u>450</u>

Explanatory Note

"Selected Countries" refers to Burma, Ceylon, India, Malaya, Pakistan, and Thailand. These countries break out transactions with Britain in their balance-of-payments data. The figures, taken from their 1962 balance-of-payments accounts, are suspect with regard to adequacy of coverage and to their comparability.

The Middle East figures are largely our estimates of income from British oil investments. The estimates are derived from data on 1963 payments by the oil companies to Middle East governments.

Although we lack data for other countries east of Suez, the amounts are probably not large enough to affect our estimated totals substantially.

There are of course debits to Britain's balance of payments which arise when British companies increase their investments abroad. These investments are assumed to be voluntary and recoverable by and large, and we have not brought them into our calculations as an offset to earnings.