MEMORANDUM FOR:

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ARGENTINA

Economic Growth Outlook

After two years of 2-3 percent gains, GDP fell at least 3 percent last year due to rampant inflation during the first half of the year and government-imposed austerity measures during the second. Economic growth of 4-6 percent in 1986 is a major goal of President Alfonsin's administration, which hopes to finance this increase in part through $2-3 billion in new lending. Zero to minimal growth is more likely, with continued stagnation of private investment this year. 25X1

Over the medium term, most econometric services project a 4-percent annual growth rate of real GDP through 1990. Such growth is easily attainable given Argentina's abundant human and natural resources, but will hinge on Alfonsin's willingness to make wide-ranging structural economic reforms to improve the investment climate and promote exports. 25X1

The External Debt

Argentina's external debt totaled $50 billion at the end of 1984, the third largest in the Third World. The vast majority of this amount is public-sector debt, and $8.9 billion is owed to US banks. Thanks to a $5.6-billion new money package from the IMF and commercial banks--$3.9 billion of which has been disbursed to date--Argentina is more or less current on its $5 billion in annual interest payments, a sum which comprises over 60 percent of its 1985 exports. 25X1

Buenos Aires has rescheduled most debt due in 1982-1985, and will soon begin negotiations on rescheduling principle maturing during 1986-1988. Argentina would also like to negotiate a new IMF stand-by agreement to replace the one which expires at the end of March. In addition, it will probably need new lending each year through the end of the decade to cover projected current-account deficits. Argentina has been active in the Cartagena group and, while rejecting calls for a debt moratorium, views some type of debt relief as necessary to ease domestic political pressures and spur economic growth. 25X1

Policy Issues

After 18 months of inflationary economic policy and confrontations with the IMF and creditor banks, Alfonsin implemented a bold stabilization program last June. Wage and price controls and tight money have cut inflation from over 25 percent per month to 2 percent. In addition, Buenos Aires was able to pare the budget deficit from a projected 7.5 percent of GDP early last year to 4 percent by year end. Argentina, however, has not made much progress in reducing the role of inefficient government enterprises, providing a favorable climate for domestic and foreign investors, and liberalizing trade policy--all prerequisites if the country is to achieve sustained growth and repay debt. 25X1

Entrenched sectors of the bureaucracy have thwarted Alfonsin's half-hearted efforts to promote private investment in the telecommunications and oil industries. Moreover, the government levied forced loans on businesses to reduce its budgetary deficit, thereby

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removing funds sorely needed for private investment. Until administration officials abandon their traditional, state-oriented approach to economic policy, business confidence is unlikely to improve and economic stagnation will probably continue. 25X1

Economy at a Glance

Argentina had a GDP of $74 billion in 1984. The country is best known for its agricultural production--it is the tenth largest wheat producer in the world and the third largest exporter. It is also a major producer of corn and other coarse grains, soybeans, and meat. In addition, Argentina supports a large industrial complex, and is self-sufficient in most manufactured goods. Key industries include food processing, motor vehicles, consumer durables, textiles, printing and metallurgy. Its most important exports are wheat, corn, oilseed, meat, hides, and wool, while its imports consist chiefly of intermediate goods such as chemicals, machinery, metallurgical products and lubricants. 25X1

Over 30 million people live in Argentina, with one-third of the population concentrated in Buenos Aires Province. In 1980 its literacy rate was 93 percent, little changed from the 91 percent posted in 1960. The country has universal primary education, and secondary school enrollment is roughly 60 percent. Argentina's basic infrastructure includes nearly 210,000 kilometers of highway, roughly a quarter of which are paved. There are also seven major and 30 minor ports, as well as 1700 airfields, of which 125 are paved. Argentina has an extensive telecommunications system. Its major natural resources include coal, with estimated reserves of 155 million metric tons, natural gas, with estimated reserves totaling 680 billion cubic meters, oil, iron, and copper. It possesses extensive deposits of radioactive materials and ranks second in the world in exports of beryllium. 25X1

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BOLIVIA

Economic Growth Outlook

President Victor Paz Estenssoro has made the overhauling of Bolivia's weak economy the major goal of his administration. Since August 1985 he has halted monetary expansion, removed price and exchange rate controls, and imposed a wage freeze that have curbed the hyperinflation inherited from the Siles Zuazo administration. [redacted] 25X1

If Paz Estenssoro is able to adhere to the agreement that he plans to sign with the IMF, we anticipate that Bolivia will substantially improve its economic performance. The IMF projects that the new program, along with additional reforms, could enable La Paz to reach 3 percent growth in 1986, with inflation below 40 percent. New funding by the IMF and rescheduling by the commercial banks should enable Bolivia to resume regular payments on its foreign debt. [redacted] 25X1

The External Debt

Bolivia's net external debt totals about $4.3 billion. About $1.1 billion represent medium and long-term obligations owed to private banks whereas another $3.6 billion is owed to official creditors. US creditors hold about $278 million of the total debt. Bolivia is currently $1.1 billion in arrears on its foreign debt servicing bill, of which 80 percent is obligated to commercial banks, 7 percent is obligated to bilateral official donors, and 3 percent is obligated to multilateral official donors. [redacted] 25X1

La Paz signed a memorandum of understanding with the IMF in December 1985 and expects to sign a standby agreement worth $50 million as early as March. It is now conducting informal talks with its Bank Advisory Committee and the Paris Club; formal negotiations for new loans and rescheduling of existing debt will commence when Bolivia reaches a final agreement with the IMF. La Paz also anticipates that additional World Bank and other multilateral assistance will be forthcoming at that time. [redacted] 25X1

Policy Issues

The Paz Estenssoro administration has instituted a stabilization program to address Bolivia's increasingly critical economic situation. Put in place in August 1985, the program includes a flexible exchange rate, raising of petroleum prices to the world level, deregulation of other prices, and a liberalization of interest rates and foreign trade. Paz Estenssoro plans fiscal reforms that include raising additional government revenue through forced loans that tax property interests of the upper class, streamlining unprofitable state enterprises, and reforming the currency. [redacted] 25X1

Several serious challenges could upset President Paz's efforts to sustain his plan even in the short term. The lifting of the state of siege in December provides organized labor more opportunity for legal protest, which will probably become more vocal and violent in the coming months as unemployment increases and austerity becomes more unpopular. The international crisis in tin, traditionally Bolivia's chief export, is adding to an already high

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unemployment rate as La Paz begins to lay off workers in state-owned mines. Paz Estenssoro retains the support of the military, but he needs to maintain the existing cooperative pact with the leading opposition party in Congress in order to push through reform legislation. Upon signing with the IMF, Bolivia will receive an inflow of funds which will ease these strains on the government. [redacted] 25X1

Economy at a Glance

Bolivia had a GDP of about $4.13 billion in 1985, according to preliminary estimates, with income per capita at about $400. The economy is concentrated largely on agriculture, manufacturing, and commerce. The agricultural sector accounts for 20 percent of GDP and 47 percent of total employment; manufacturing accounts for 15.5 percent of GDP and 11.6 percent of employment; commerce produces 15 percent of GDP and accounts for 8 percent of employment. The country's main crops include potatoes, corn, rice, sugarcane, coca, yucca, bananas, and coffee; La Paz imports significant quantities of wheat. Agricultural development in Bolivia is constrained because the bulk of the population lives in the unproductive altiplano region, where the weather is harsh, extremely small holdings of land predominate, and the infrastructure is underdeveloped. Major industries include mining, smelting, petroleum refining, food processing, textiles, and clothing. Most industries are concentrated in La Paz, with many plants in Oruro and Potosi. Dominant exports include natural gas, tin, and other metals. Falling world prices for these exports and, until recently, its fixed exchange rate hurt potential export income by making Bolivian exports more expensive relative to those of other countries. [redacted] 25X1

Bolivia has a population of 6.3 million. Its literacy rate is estimated at 63 percent. Education is universal, free, and compulsory until age 14; enrollment in secondary schools is currently about 13 percent. The country's basic infrastructure includes 38,830 kilometers of highway, of which 30,836 kilometers are unpaved. Bolivia also has 3,651 kilometers of railroad, 10,000 kilometers of navigable inland waterways, and 564 airfields, of which nine are permanently paved. The country has a limited telecommunications system, with an inadequate radio-relay system, an average two telephones per person, 172 radio stations, and 43 television stations. Bolivia has vast mineral deposits which contribute nine percent of GDP but are of major importance in the export sector. Mineral deposits include tin, silver, gold, petroleum, natural gas, lead, antimony, tungsten, zinc, copper, and bismuth. [redacted] 25X1

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BRAZIL

Economic Growth Outlook

The Sarney government, with an eye to bolstering its popular support, has made economic growth its major goal. In 1985, the relaxation of fiscal discipline, real wage increases, and a record agricultural harvest spurred real economic gains of 7-8 percent, the highest level since 1976. Despite the boom and inflation that hit 235 percent the trade surplus held up at $12.5 billion. [redacted] 25X1

Over the medium term, most econometric services project that Brazil's performance will fall below the government's target of 6 percent real annual growth. Industrial capacity constraints, the likelihood that inflation will remain above 200 percent, and depressed new investment will all brake the economic advance. Nonetheless, government spending to develop the resource base and improve social welfare will probably enable Brazil to record 3 to 4 percent annual increases in real growth through 1990. [redacted] 25X1

The External Debt

Brazil's external debt totals about $103 billion, the largest in the Third World. About $75 billion represent medium-term obligations owed to private banks at floating rates, whereas another $15 billion is owed to official creditors on fixed repayment terms. US creditors hold about $25 billion of total debt. Brazil is currently up to date on its estimated $10 billion annual interest payments,--a sum that represents 40 percent of 1985 merchandise export--but still had to reschedule $7 billion in 1985 principal repayment. [redacted] 25X1

Brasilia has indicated it will not adopt the anti-inflationary measures considered essential by the IMF, and has no standby agreement. Consequently, negotiations are on hold for a multi-year restructuring of its commercial debt while official debt rescheduling through the Paris Club is in limbo. The government's present plan is to seek a rescheduling of 1985-86 maturities and to rollover $16 billion in short-term credit lines by working out some type of informal agreement with the IMF. Additionally, Brasilia is becoming more active in seeking financial concessions from creditors under the aegis of the Cartagena group and is known to favor some form of interest payment relief to resolve the region's debt difficulties. [redacted] 25X1

Policy Issues

The Sarney administration is adopting a gradualist and anti-monetarist approach to Brazil's serious economic problems. The 1986 economic program calls for a moderate reduction of the public-sector deficit, mainly with higher taxes and lower interest rates versus spending cuts. Increasingly, the government will print currency to finance the deficit, contain domestic debt, and lower domestic interest rates. Although the government is opposed to granting substantial additional real wage hikes, it probably will give in to rising labor activism in this important election year. To contain inflation, Brasilia will continue to use price controls, tighten consumer credit, and restrain the rate of monetary adjustment. Additionally, imports of selected products will be allow to expand to sustain growth and hold down food price increases caused by the current drought, the government will attempt to continue devaluations to match the rate of inflation to keep exports competitive and to post another large trade surplus. [redacted] 25X1

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The failure to undertake structural reform, however, will lock in serious imbalances that restrain the economy's long-run growth potential. For example, persistent public deficits are driving Brazil's domestic debt to dangerous levels, crowding out private sector borrowers, and thwarting capital market reform necessary to bring down punishing real interest rates. Until the indexation system is dismantled, inflation will remain in triple-digits, undermining new capital formation. Real wage increases will exacerbate the price-spiral and threaten to hurt Brazil's export competitiveness. Although the government has announced plans to sell nonvoting shares of public enterprises, it refuses to relinquish the control to the private sector that would be necessary to improve the parastatals' operating efficiency. Moreover, Brasilia still remains opposed to a major liberalization of the foreign investment code of the sort required to attract new direct investment. 25X1

The Economy at a Glance

Brazil had a GNP of $212 billion in 1984. As recently as a decade ago, agriculture accounted for 12 percent of GDP and manufacturing 19 percent. Since that time the reliance on manufacturing has grown to 27 percent. Major crops include coffee, rice, corn, sugarcane, soybeans, cotton, manioc, and oranges. Despite this range of output the FAO estimates that nearly 70 percent of the land area suitable for farming is not being used. Moreover, existing agriculture techniques are still primitive and rely heavily on slash-and-burn clearing and riverbank planting. The potential for mechanization is thus great. Major industries include textiles and other consumer goods, chemicals, cement, lumber, steel, motor vehicles, other metal working industries and capital goods. Industrial development is concentrated in the southeast, particularly in Sao Paulo, which is the largest and most modern industrial complex in Latin America. Brazil has the largest and oldest steel industry in Latin America with more than 50 steel mills. The automotive industry, the fifth largest in the world, is almost entirely controlled by private enterprise. Other dynamic manufacturing industries in the 1970s were chemicals, pulp and paper, electronics and electrical goods, steel, and footwear. As far as exports are concerned soybeans, coffee, transport equipments, iron ore, steel products, chemicals, machinery, orange juice, shoes, and sugar have dominated. 25X1

Brazil has a population of nearly 138 million. In 1980 the literacy rate was 76 percent. Over 90 percent of all children are enrolled in primary schooling, and the number enrolled in secondary school stands at over 30 percent. As far as the basic infrastructure is concerned, the country has about 1.4 million kilometers of highways, under 10 percent of which are paved. Brazil also has 50,000 kilometers usable inland waterways. Moreover, it has 8 major ports and 23 significant minor ports. In addition, the country has nearly 4,000 usable airfields with 300 having permanent surfaced runways. Brazil has a good telecommunications system and extensive radio relay facilities. As far as minerals are concerned, iron ore and manganese are the most important minerals produced in the country. Known minerals are concentrated in the state of Minas Gerais, believed to contain 7 billion tons of high-grade iron ore and 24 billion tons of low-grade ore, representing one-fifth of the world's known reserves. Brazil also contains 80 percent of Latin America's managanese. Other minerals resources include bauxite, copper, gold, lead, magnesite, diamonds, nickel, silver, tin, tungsten, and asbestos. Recent discoveries of platinum are believed to contain half of the known reserves of the mineral in the world. 25X1

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CHILE

Economic Growth Outlook

The Pinochet government is attempting to spur economic growth by adopting an export-oriented economic restructuring program. Despite strong fiscal discipline and moderate monetary policies in 1985, an earthquake, adverse export prices, and delays in loan disbursements kept growth near Chile's 1.7 percent population growth. Nevertheless, Santiago almost tripled its trade surplus compared to 1984, with only a minor rise in inflation. 25X1

Over the medium term, most econometric services project that Chile will not attain the government's projection of 3-5 percent real annual growth. Depressed commodity prices, low domestic savings, and foreign creditor reluctance to finance investment activity will likely contribute to a sporadic economic performance over the next several years. Nevertheless, government rationing of scarce credit to industries and increased borrowing from international financial institutions will help Chile average 2-3 percent real growth through 1990. 25X1

The External Debt

Chile's external debt totals $22 billion, one of the highest per capita debt levels in Latin America. Over $14 billion represent medium-term obligations to private banks at floating rates, and $2 billion is owed to official creditors on fixed repayment terms. US creditors hold about $7 billion of the total debt. Chile is currently up to date on its estimated $2 billion annual interest payments--a sum that represents about 56 percent of 1985 merchandise exports--and is rescheduling 1985-1986 maturing debt. 25X1

Chile has reaffirmed its intention to comply with the conditions of its IMF program and World Bank loans. Consequently, the IMF may loosen macroeconomic targets for 1986 to help Santiago spur stronger growth. Despite new lending by international financial institutions, Santiago will probably start rescheduling talks for maturing 1987-1990 debt later this year in order to keep current on its debt service past 1986. Adverse international commodity prices, rising interest rates, or domestic political pressures for greater growth could prompt Santiago to seek additional loans. Should bankers reject a request for another rescheduling or more loans, Santiago might become more active than it has been in the Cartegena group. 25X1

Policy Issues

Chile's inflation rate will remain around 25 percent over the next several years as the government maintains moderate monetary expansion and trade-competitive devaluations. However, interest rates will remain low, hurting prospects to finance future growth from domestic investment. Weak unions and tight government control over public-sector wage rates will prevent real wage growth during the next several years. Santiago's moves to sell publicly controlled corporations to the private sector will be slowed by the dearth of domestic buyers and by foreign investors' nervousness over Chile's political future. The government intends to balance its external accounts and promote exports by protecting domestic producers and encouraging trade diversification with subsidies. 25X1

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[redacted] 25X1

Chile's efforts to restructure its economy bode relatively well for the future; nonetheless, social and political strains could derail the program. Increasing political restiveness could unnerve bankers and foreign investors, jeopardizing the foreign financing Santiago needs to undertake its reforms. Moreover, Pinochet may spur faster economic growth for short-term political gains at the expense of scuttling the restructuring program. [redacted] 25X1

Economy at a Glance

Chile had a GDP of $19.2 billion in 1984. Services generate over half of GDP, agriculture accounts for 10 percent and industry for 36 percent. Major crops include wheat, potatoes, corn, sugar, beets, onions, beans and fruits. Price supports in the last several years have brought about a resurgence in the agricultural sector and Chile will become a net food exporter in 1986. Major industries include copper, foodstuffs, fish processing, iron and steel, pulp, paper, and forestry products. Chile plans to nearly double its copper production between 1983-1993. Domestic crude oil production fell in 1985, but coal production and new investments in gas will help hold down domestic petroleum consumption. The fishing industry--the third largest in the world--enjoyed a good year in 1985 and improving fish stocks portend continued growth over the next several years. Forestry products, such as paper pulp, have also grown. Although copper remains the largest export at around 43 percent of the total, forestry and fish products, and fruits and vegetables now comprise 36 percent of exports. Although the volume of these non-traditional exports has increased, falling commodity prices have suppressed the rise in export revenues. [redacted] 25X1

Chile has a population of nearly 12 million. Its literacy rate exceeds 90 percent. Government emphasis on education has encouraged adults to take primary education courses, swelling enrollment by 1982 to 112 percent of the normal school age population. The country has over 78,025 km of highways of which over 12 percent are paved. Chile has 2,000 km of navigable inland waterways, and has 10 major ports along its 6,435 km coastline. In addition, the country has 320 usable airfields with 46 permanently paved. Chile has a good telecommunications system and is part of the Intelsat and Inmarsat systems. Copper, gold, molybdenum, iron ore, silver, nitrates, lithium and iodine are the most important minerals produced in the country. Chile contains one-fifth of the world's known copper reserves and has been the world's largest copper producer since 1982. [redacted] 25X1

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COLOMBIA

Economic Growth Outlook

The free market-oriented Betancur government has pursued expansionist economic policies since August 1982 to improve Colombian living standards. Pressures for economic adjustments peaked in early 1985 when foreign bankers refused to lend without an IMF program in place. With seven months left in Betancur's term, economic growth remains relatively stagnant at around 2 percent. 25X1

Most forecasters agree that Colombia's economic growth will pickup this year and will probably average 4 percent annually through 1990. The country's external accounts, helped by an export surge in petroleum, coal, and coffee, should be among the healthiest in Latin America after 1987. Despite the projected upturn, forecasters see unemployment remaining at the current record of 15 percent and inflation stubbornly high in the 18 to 25 percent range per year through 1990, reflecting widespread uncertainly over economic adjustments that extend beyond the Betancur era. 25X1

The External Debt

Unlike other major South American countries, Colombia has serviced its $12 billion medium- and long-term foreign debt without rescheduling. Because of its success in managing its financial obligations, Bogota has lower interest rates and longer repayment terms for approximately 40 percent of the $8 billion debt it owes international agencies such as the World Bank and the Inter-American Development Bank. Colombia owes approximately 35 percent of the nearly $5 billion in public-sector commercial loans to US banks. Although the public sector is generally current in servicing its obligations, the private sector is encountering difficulty because of the acceleration of monthly currency devaluations and cash flow problems. Total private foreign debt has increased to $4 billion, including some $1.2 billion in expensive short-term obligations. Most private debt is owed to US banks. 25X1

Bogota has submitted to IMF monitoring in order to obtain the $1 billion loan it requested from international bankers a year ago. Quarterly disbursements will begin this year after the Fund issues its first report on economic performance. The World Bank has already disbursed part of a $300 million loan to finance Colombia's export diversification. Betancur hosted the first meeting of the Cartagena Group in June 1984. He does not advocate the formation of a debtors' cartel, but has campaigned for easier repayment terms, more lending, and a regional approach to the debt issue. 25X1

Policy Issues

The Betancur government is implementing, slowly and selectively, a two-year self-imposed, IMF-monitored stabilization program that is similar to a formal IMF standby accord, but more appealing to the country's political elites. Consequently, progress toward economic adjustment has been measured. As of 30 September 1985, Colombia was meeting economic targets recommended by the IMF with two exceptions: inflation and net changes in international reserves. Since early 1985 Betancur has increased gasoline prices, bus fares,

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and value added taxes, cut government spending, limited wage increases, lifted some import restrictions, and stepped up the rate of currency devaluation. [redacted] 25X1

The success of this approach to austerity depends upon the continued cooperation of political parties, business groups, and labor along with government self-discipline in following through with promises to cut public works projects and hold down wages. Moreover, a sudden drop in world oil or coal prices, or a massive capital flight could force a larger-than-expected drawdown of foreign exchange reserves straining Colombia's ability to service its debt. [redacted] 25X1

Economy at a Glance

Colombia had a GNP of $29 billion in 1985. Over the last 20 years, the importance of agriculture has declined substantially. In 1960, over 50 percent of the work force was employed in agriculture. By 1981 that figure had been cut in half. Colombia's main crops are coffee, rice, corn, sugarcane, marijuana, cocoa, plantains, bananas, cotton, and tobacco. Major industries include textiles, food processing, clothing and footware, beverages, chemicals, metal products, and cement. There are three major industrial centers in the country: Bogota, Cali, and Medellin. In an effort to broaden the benefits of industrial development, the government offers financial incentives including lower minimum wage rates to new industries locating in less populated areas. Consequently, many new industries are being established in such cities as Cartagena, Barranquilla, Manizales, and Barrancabermeja. Almost two-thirds of manufacturing output consists of consumer goods, and one-third of intermediate capital goods. Most of the newer industries are chemical, paper, mechanical and electrical equipment, and metalworking. Sugar refining alone accounts for around 15 percent of employment. The second largest sub-sector is textile production. There are also a number of automotive assembly plants owned by Chrysler, Renault, and Fiat. Key exports include coffee, fuel oil, cotton, tobacco, sugar, textiles, cattle and hides, banana, and fresh cut flowers. [redacted] 25X1

Colombia has a population of a little over 28 million. In 1984 the literacy rate was 80 percent, up nearly 20 percentage points since 1960. The country has universal primary education and 50 percent of secondary school-aged youth are enrolled. As far as basic infrastructure is concerned, the country has over 75,000 kilometers of highways, less than 15 percent of which are paved. There are six major ports and over 600 usable airfields, 10 percent of which are permanently surfaced. The country has a nationwide radio-relay telecommunications system. Colombia's major non-oil mineral resources are coal, copper, iron ore, nickel, antimony, bauxite, emerals, and gold. Colombia is the largest coal producer in South America, possessing more tha 40 percent of the region's coal reserves, approximately 16 billion metric tons. Colombia also is the source of 95 percent of the world's gem emeralds, and it is South America's only producer of platinum and the second largest producer of gold. Its oil reserves are the third largest in Latin America. Uranimum deposits have been discovered in Santander. Copper deposits estimated at 625 million tons are located in Pantanos. Exploitation of the vast Cerromatoso nickel resources, estimated at 70 million tons, began in 1970. [redacted] 25X1

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ECUADOR

Economic Growth Outlook

President Febres-Cordero has sought to stimulate growth through free market initiatives which reduce subsidies, decrease regulation, and open some sectors of the economy to increased competition. As a result of these reform policies, total investments expanded by 40 percent and exports by 8 percent in 1985, and Ecuador recorded a trade surplus of almost $1 billion last year. 25X1

Ecuador's economic prospects appear favorable--barring a sudden decline in world oil prices--with annual growth projected at the rate of at least 4 percent per year from 1986-1990. Oil revenues will remain the mainstay of export earnings and public sector revenues, but the growth in non-oil exports--up 29 percent in 1985--will probably continue. A severe drop in oil prices, however, would cut into export earnings and greatly complicate Quito's ability to comply with IMF targets--a public sector surplus equal to 3.4 percent of GDP and elimination of the balance of payments deficit. Moreover, a resurgence of domestic inflation could jeopardize Febres-Cordero's free market strategy by forcing tighter monetary policies and discouraging the investment necessary for growth. 25X1

The External Debt

Ecuador's external debt totals $8.4 billion, making it one of the region's smaller debtors in absolute terms but one of the larger debtors in per capita terms. Commercial banks hold about $5 billion in Ecuador's medium and long-term debt, at floating rates, and about $1.4 billion in short term debt, also at floating rates. Ecuador owes $2.1 billion to US banks, 33 percent of its bank-held debt. Official creditors hold another $2 billion of Ecuador's debt, most of it long-term and at fixed repayment terms. Quito is current in servicing its external debt obligations. 25X1

Quito achieved new debt agreements with both official and bank creditors in 1985. Quito reached agreement with the IMF in March on the terms for a $100 million stand-by facility and concluded negotiations with the Paris Club in April for a 3-year rescheduling of its debts to official agencies. In late 1985 Quito also rescheduled $4.3 billion in commercial bank debts falling due between now and 1989. These refinaning agreements lower Ecuador's debt service ratio from 60 percent of exports to 33 percent and ease the pressure on Ecuador's foreign exchange reserves. 25X1

Policy Issues

Despite these impressive achievements, economic policy choices could pose trouble for Febres-Cordero in the near term. The principal challenge, in our view, will be meeting IMF targets--the lynchpin of good relations with creditors. Quito agreed with the IMF to reduce inflation to 20 percent and will likely maintain tight liquidity to achieve that target. Interest rates will remain high. Any surge of inflation would require even tighter monetary policies and rising interest rates could derail the new investment Quito seeks to attract. In addition to restricting Central Bank credit, Quito could be compelled to return to price controls, further

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damping free market initiatives for investment spending. A failure of private investment would also threaten IMF-agreed budget goals by causing an economic slowdown and producing domestic political pressure for the administration to increase spending. Without growing private investment, Quito cannot hope to achieve its growth or IMF-mandated budget targets. [redacted] 25X1

· Febres-Cordero's liberal trade and investment policies could also be threatened by domestic criticism. Administration moves to remove tariffs, lift protectionist bans on manufactured imports, and stimulate foreign investment could lead to a surge of imports and raise domestic demands for lower imports and foreign investment flows. [redacted] 25X1

Economy at a Glance

Ecuador had a GDP in 1985 of $12.9 billion, equal to $1,440 per capita. Agriculture accounts for 14 percent of GDP, industry 35 percent, services 38 percent, and public administration 7 percent. Major crops include bananas, coffee, cocoa, sugarcane, corn, potatoes, and rice. The relative decline of agriculture is of serious concern to Quito and the government is reducing subsidies and removing price controls in this sector to improve growth prospects. Major industries include petroleum, food processing, textiles, chemicals, and fishing. The petroleum sector grew 12 percent in 1984 but slowed to a 4 percent rise in 1985 as lower oil prices hurt Ecuador's ability to market crude oil. Nevertheless, Ecuador closed 1985 with production near 300,000 barrels per day. Manufacturing grew little in 1984 or 1985, but utilities grew at 13 percent and construction at 1 percent in the two-year period. We expect growth to fall in 1986 in the utilities and construction sectors-and perhaps the services sector-due to Quito's tight monetary policies. But the government expects significant recovery in both manufacturing and construction. Exports reached $2.73 billion in 1985, with oil and oil products ($1.9 billion), bananas ($194 million), fish ($183 million), and coffee ($179 million) leading the way. Major trade partners are the US (49 percent), Latin America (20 percent), and Japan (7 percent). [redacted] 25X1

Ecuador's population is approximately 9.0 million, with annual growth at 2.7 percent. The literacy rate is 84 percent. The labor force contains 2.8 million people, with 52 percent in agriculture, 13 percent in manufacturing, 7 percent in commerce, 4 percent in construction, 4 percent in public administration, and 16 percent in other services and activities. Ecuador's basic infrastructure is reasonably well developed, with 2,000 kilometers (km) of railroads, 69,000 km of roads--about half of which are paved or graveled, 1,500 km of navagible waterways, 2,260 km of oil pipelines, 3 major habors, and 166 airports--23 with permanent-surface runways. [redacted] 25X1

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PARAGUAY

Economic Growth Outlook

Paraguay had a positive growth rate of 3.0 percent in 1985, recovering from a recession in the early 1980s. Recent economic gains resulted largely from improved agricultural performance, especially bountiful soybean and cotton harvests. Moreover, there was growth in the service sector stemming from increased tourism. The central bank's loose credit policy over the past two years also facilitated economic expansion. 25X1

Paraguay's economy, however, is likely to take a downward turn in the coming year. The overvalued exchange rate, low international prices for Asuncion's agricultural exports, and a crippling drought threaten to reduce growth below the 3 percent range during 1986. The Central Bank has begun to restrict bank credit to compensate for excessive monetary emissions in 1985. In addition, a decline in foreign investment and continuing delays with a multibillion dollar hydroelectric project--a major source of revenue--further bleaken Paraguayan economic prospects. 25X1

The External Debt

The registered foreign debt is approximately $1.8 billion. About 90 percent represents Paraguay's long term debt, the majority of which belongs to the public sector. Last year, Asuncion paid $227 million in interest and principle, a sum representing 45 percent of the country's annual merchandise exports. In effort to conserve its reserves, Paraguay has incurred interest arrearages estimated at over $250 million. A balance of payments deficit of $150 million projected for 1986 could cause arrearages to worsen and foreign reserves to fall below $300 million. 25X1

Although Paraguay has so far avoided an IMF stabilization program, foreign creditors are growing reluctant to lend new money because of the country's repeated failure to meet its payments. The IMF and other foreign lenders have been pressing President Stroessner for a thorough adjustment of the national economy. The World Bank recently stopped lending to Paraguay in response to debt arrearages and disagreement over the exchange rate for loan disbursements. Asuncion's deteriorating payments position will likely become so untenable during 1986 that Paraguay may have little choice but to reach an agreement with the Fund and reschedule its debt with creditor banks. 25X1

Policy Issues

President Stroessner's policies are providing scant relief for Paraguay's economic problems. Stroessner has tightened monetary policy to compensate for the decline in foreign reserves and has begun to crack down on import abuses. He continues, however, to reject proposals from economic advisors and international financial institutions for further reforms, such as revamping the tax system and enacting export-promotion measures. The economic horizon is also clouded by political uncertainty. Stroessner, 73, has been in office for 31 years and has no clear successor. Fear of the political and economic consequences of his sudden incapacitation or death will continue to hamper domestic private and foreign investment until ground rules for the post-Stroessner era emerge. 25X1

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The country's economic outlook is also jeopardized by the overvalued currency and multiple exchange rate policy. The parallel market rate for the guarani is approximately four times the official rate. Stroessner, however, refuses to devalue, believing that political stability is directly related to the stability of the currency. Another factor bolstering the current exchange rate policy is the corruption that permeates the government. Many high level officials personally profit from the guarani's artifically low rate. In addition, failure to adjust the exchange rate is undermining domestic confidence in the guarani, spurring large dollar withdrawals from banks, and increasing capital flight. Capital flight will accelerate as long as the exchange rate remains unchanged, putting further pressure on Asuncion's already depleted stock of foreign reserves. 25X1

Economy at a Glance

Paraguay had a GDP of 3.8 billion in 1984. Although less than 2% of the land is cultivated, Paraguay has an agricultural based economy and is self-sufficient in most foods. Agriculture and livestock account for 95% of the country's export earnings. Main crops include cotton, soybeans, oilseeds, corn, rice, sugarcane, tobacco, wheat, manioc, and sweet potatoes. Industry is limited to processing of agricultural products and small scale manufacturing of consumer goods, including meat packing, oilseed crushing, milling, brewing, and textiles. Paraguay must import most industrial and manufactured goods, such as machinery, motor vehicles, and fuels and lubricants. However, Paraguay boasts the largest hydroelectric project in the world--the Itaipu dam, a joint venture with neighboring Brazil. Other joint hydroelectric projects are planned with Argentina. Once these are completed, Paraguay will be the world's leading exporter of electricity. 25X1

Paraguay has a population of 3.7 million, 70 percent of which is age 25 or younger. Virtually the entire population is mestizo of mixed Indian and European descent. The literacy rate is estimated at 81%. Paraguay's basic infrastructure includes approximately 22,000 km of roads, but only 2,000 km are paved. The country is landlocked, its sole access to the sea being the river ports of Asuncion and a few other cities. Paraguay has 769 usable airfields, but only six have surfaced runways. Telecommunications are mostly concentrated in Asuncion and a few major cities. The only mineral mined in Paraguay is limestone, although there may be oil deposits in the Chaco region, near the Bolivian border. 25X1

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PERU

Economic Growth Outlook

President Alan Garcia has moved swiftly to implement nationalistic economic policies to restore growth, improve social welfare, and reduce dependency on foreign investment. Price controls have slowed the rate of inflation--which peaked at 184 percent in August 1985--but food shortages have developed, and economic growth remains sluggish. [redacted] 25X1

Most econometric services forecast a growth rate of below 4 percent for Peru's economy through 1990, allowing for only a slow recovery in the standards of living. Political and economic uncertainties are likely to discourage domestic and foreign investment, and Garcia will be hard put to control inflation unless he can drastically reduce the government's fiscal deficit. The increasingly bleak outlook for this world oil market for at least the next two years, together with generally weak world prices for key commodity exports expected through 1990, will yield meager export earnings, and Garcia is unlikely to authorize more than token payments for Western creditors unless bankers agree to greatly liberalized terms for the repayment of Peru's debt. [redacted] 25X1

The External Debt

Peru's external debt to Western creditors totals $14 billion. About $8 billion represents medium and long-term obligations owed to private banks at floating rates, whereas another $6 billion is owed to official creditors on fixed repayment terms. US banks hold about $3.5 billion of total debt. Peru's total debt-servicing obligations in 1985 exceeded $2.5 billion. Lima is over $300 million in arrears on its estimated $1 billion annual interest payments for 1985, a sum that represents 33 percent of last year's export earnings. Morever, Lima has yet to reschedule its 1984 debt to international bankers and the Paris Club. Peru's debt to the Soviets, who willingly accept goods as payment, amounts to $2 billion. [redacted] 25X1

Garcia views debt primarily as a political issue because it inhibits the initiation of social welfare programs which he regards as necessary to prevent political unrest. He remains committed to limiting debt servicing to 10 percent of export earnings through August 1986 and by passing the IMF. Relations with Western creditors are strained and Garcia's refusal to back away from his hard line on debt has increasingly isolated Peru from international lenders. Lima has publicly promoted joint action among Latin American debtors to secure easier repayment terms. [redacted] 25X1

Policy Issues

Although the approach has been piecemeal, the overall thrust of Garcia's economic program has been in the direction of a self-imposed stabilization program, similar to those in Colombia and Venezuela, that would win support from foreign lenders without the need for a formal IMF adjustment program. Since August 1985 Garcia has lowered domestic interest rates, frozen rents, and put price controls on basic consumer goods in a politically popular attack against three-digit inflation inherited from the Belaunde administration. He also has frozen U.S. dollar deposits and imposed controls on imports to protect industry and foreign

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exchange. Garcia, in addition, has reduced salaries of top officials, frozen government hiring, indicated his interest in slashing defense expenditures, and begun restructuring the agricultural and oil bureaucracy to reduce the budget deficit. In an apparent step to implement his nationalistic foreign investment policies, he also has taken over a US oil firm that failed to accept Lima's requirements for additional exploration, profit sharing, and new tax arrangements. Another US oil company and a US-Argentine consortium will be allowed to stay in Peru, however, contingent on approval of some final agreements. 25X1

If Garcia sticks with his reform program and improves the tenor of his government's dealings with bankers, the current impasse between Peru and its creditors may fade. A resurgence of inflation, however, could lead Garcia to opt for growth and job creation, particularly if his popularity were to slide, and such tactics would make a reconciliation with Western creditors even more difficult. 25X1

Economy at a Glance

Peru had a GNP of just under $17 billion in 1984. The country has a fairly well diversified economy. Both agriculture and services account for 40 percent of overall employment, while industry represents the remaining 20 percent. The country's main crops include wheat, potatoes, beans, rice, barley, coffee, cotton, and sugarcane. Fish is also important. Of the areas being cultivated, most of the coastal farmland is devoted to export crops, and the Sierra and Selva farms are devoted to food crops. Cultivation in the coastal region is limited to river valleys and irrigated areas because of the almost complete absence of rainfall. This places irrigation capability at a premium. Major industries include the mining of metals, petroleum, fishing, textile and clothing, food processing, cement, automobile assembly, steel, shipbuilding, and metal fabrication. The manufacturing sector is the fastest growing portion of the economy and production is heavily concentrated in the Lima-Callao area, where nearly 65 percent of all plants are located. Government efforts to attract industries to other parts of the country have included the construction of industrial parks in Trujillo, Arequipa, Tacna, Cuzco, and Huancayo. The expansion of the fish-meal industry has stimulated the establishment of a number of spinoff industries such as boatyards and plants for the production of nylon fish nets. As far as exports are concerned, copper, fish and fish products, silver, iron, cotton, sugar, lead, zinc, petroleum, and coffee dominate. 25X1

Peru has a population of over 19 million. In 1980 the literacy was 80 percent, up roughly 20 percentage points since 1960. The country has universal primary education, and the level of enrollment of secondary school-aged youth stands at nearly 60 percent. As far as basic infrastructure is concerned, Peru has over 56,000 kilometers of highway, however, roughly half are unimproved. There are also seven major and 20 minor ports, as well as over 230 airfields, 29 of which are permanently surfaced. The country's telecommunications system is rated as fairly adequate for most requirements and includes a nationwwide radio-relay system. As far as minerals are concerned, Peru mines 20 metals, and 20 nonmetalic minerals. Almost all of the mining activity is centered in the central Sierra at elevations varing from 3,000 to 4,900 meters. The principal metals are copper, iron ore, lead, zinc, and silver. Known copper reserves are estimated at 1.3 billion tons and Peru ranks sixth in the world's annual copper exports. Proven oil reserves equal 700 million barrels and 1985 production reached 180,000 barrels per day, one third of which was exported. In the

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mid-1970s, 3 billion tons of coal were discovered in Peru and the country is also blessed with huge, relatively untapped phosphate deposits in the Sechura Desert. 25X1

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URUGUAY

Economic Growth Outlook

President Julio Sanguinetti is counting on further liberalization of the basically free market economy to ease foreign debt difficulties as well as address popular demands for economic growth. Progress in this area has enabled Montevideo to reach agreement with the IMF and its commercial creditors, but a domestic economic turnaround has not yet materialized. 25X1

Uruguay will be hard pressed to overcome the effects of its five-year recession, and growth will probably average no more than one to two percent per year over the medium term. World prices for its mostly agricultural export products are bearish, which will continue to depress export revenues. Investment will also be limited by difficulties in accumulating private and public savings, further hampering industrial and agricultural recovery. 25X1

The External Debt

Uruguay's net external debt totals about $3.8 billion, the largest per-capita debt in the Third World. About $2.5 billion represents medium and long-term obligations owed to private banks. US creditors hold about $1 billion of total debt. Montevideo is currently up to date on its estimated $370 million annual interest payments, a sum that represents 46 percent of 1985 merchandise exports. 25X1

Uruguay signed a financial assistance package in September 1985 that provides for $120 million in IMF funds to be disbursed over 18 months as well as $150 million in new loans from other lenders. Creditors also granted a graduated repayment schedule with lower interest rates and a three-year grace period. Foreign Minister Enrique Iglesias, secretary pro tem of the Cartagena Group, has publicly called for political solutions to ease Latin American countries' repayment burdens but does not advocate a debtors' cartel or debt repudiation. 25X1

Policy Issues

The Sanguinetti administration favors a market-oriented approach to fueling domestic economic recovery and improving the external accounts. Uruguay's export promotion program includes a freely-floating exchange rate and a set of export incentives for local producers. Montevideo is also moving to reduce the budget deficit by holding the central government's expenditures constant, increasing revenues from the value-added tax, and implementing strict new tax collection procedures. These improvements in public finance have enabled Uruguay to reduce its rate of monetary expansion and hold inflation to 82 percent in 1985. 25X1

These reforms are helping to pull Uruguay out of recession, but have not generated significant economic growth. As the economy continues to stagnate over the next year, Sanguinetti's social consensus will begin to erode, with political opponents calling for growth-promoting policies, organized labor demanding wage hikes, and the military lobbying

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for increased defense spending. Private businessmen will also demand an easing of their huge debt burdens--brought on by falling demand and lack of investment--and Montevideo's tight monetary policy will make credit scarce and expensive. Sanguinetti may then seek to placate the opposition by pursuing more rapid, inflationary growth that would threaten Uruguay's compliance with the IMF. [redacted] 25X1

The Economy at a Glance

Uruguay had a GDP of $5.147 billion in 1984. The economy is concentrated largely in services, which represent more than 60 percent of both labor force employment and overall GDP. The industrial component accounts for a third of overall employment and value-added. The country's main crops include wheat, rice, corn, and sorghum. Uruguay is self-sufficient in most basic food stuffs; about 73 percent of the land area is devoted to raising livestock, which provides more than two-thirds of total agricultural production. Major industries include meat processing, wool and hides, textiles, footwear, leather apparel, tires, cement, fishing, and petroleum refining. Most industries are concentrated in the Montevideo area, and smaller centers are found in Paysandu, Rio Negro, Lavallejo, Artigas, and Colonia. Dominant exports include wool hides, meat, textiles, leather products, fish, and rice. [redacted] 25X1

Uruguay has a population of 2.9 million. In 1984 the literacy rate was 94 percent, up slightly from the 87 percent rate of 1960. The country has universal primary education, and enrollment in secondary schools is running at about 60 percent. Uruguay's basic infrastructure includes nearly 50,000 kilometers of roads, of which 40,000 are dirt. The country also has one major and nine minor ports, as well as 108 usable airfields, 13 of which are paved. Uruguay has an adequate telecommunications system, with most modern facilities concentrated at Montevideo. In addition, it has a new nationwide radio-relay network. The country's mineral deposits--including manganese, iron, lead, copper, ilmenite, rutile, zircon, and monazite--are limited, and production is insignificant. [redacted] 25X1

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VENEZUELA

Economic Growth Outlook

The Lusinchi administration, facing unprecedented levels of unemployment and national elections in 1988, has made economic recovery its primary goal. In 1985, however, delays in implementing new public investment programs and a continued shortfall of private investment--which was exacerbated by sagging oil revenues--held real growth flat, resulting in a seventh consecutive year of economic stagnation. Weak domestic demand caused inflation to fall to 7 percent while lower-than-expected imports and falling interest rates produced a current account surplus of $4 billion. [redacted] 25X1

Over the medium term, most econometric services project steady recovery. Increased public spending, modest real wage gains, and continued import substitution behind tight import barriers are expected to increase real annual growth to 4 percent by 1990. Nonetheless, a sharp drop in world oil prices--petroleum accounts for 25 percent of GNP, 70 percent of government revenues, and 90 percent of exports--would derail recovery and bring on resurgent debt repayment problems. [redacted] 25X1

The External Debt

Venezuela's external debt is an estimated $33 billion, the sixth largest in the Third World. It is owed primarily to commercial banks, with US creditors holding one-third of the total. Nearly $25 billion represents public sector obligations while the external private debt is at least eight billion dollars. Since President Lusinchi's inauguration, interest arrearages on the public debt have been eliminated, although some arrearages on the private external debt persist. Total interest outlays for 1985 are said to have been $3.8 billion, about 27 percent of merchandise exports. [redacted] 25X1

Venezuela's tough, self-imposed stabilization program and cooperative attitude toward creditors is paying dividends. Currently, Caracas is in the process of finalizing a multi-year restructuring of $21 billion of the external public debt which will reduce scheduled principal repayments from a peak of nearly $5 billion in 1985 to an annual average of $1.6 billion through 1990. Under the terms of the agreement, Venezuela can call for another restructuring of its debt in the event of a major decline in oil prices. Consequently, Venezuela is a voice of moderation in the Cartagena group and favors nonconfrontational tactics in dealing with creditors. [redacted] 25X1

Policy Issues

The Lusinchi administration is facing growing domestic pressures to reactivate the economy. With debt rescheduling almost completed, the government has adopted an ambitious investment program to provide the economy much needed fiscal stimulus and drawdown two years accumulation of budgetary surpluses. The Government has indicated that it will continue its accommodative monetary policy. Additionally, real wage restraint has been relaxed in an effort to retain support of the vital labor constituency and boost domestic demand. Caracas will continue price controls to restrain price rises. Because the swing to a

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more expansionary strategy will strain the external payments accounts, import licensing and foreign exchange controls are being retained to limit the outflow of foreign exchange. 25X1

Uncertainty over oil exports and the government's reliance on extensive economic controls continues to discourage the private investment necessary to promote economic recovery in the medium term. Price controls, for example, have made profit prospects in certain industries problematic, while recent efforts to liberalize the foreign investment code have been half-hearted and are unlikely to attract much interest among investors abroad. Meanwhile, stiff import licensing requirements are protecting inefficient domestic producers in many industries. The key factor depressing investor confidence, however, is the dismal outlook for oil revenues. 25X1

The Economy

Venezuela had a GDP of about $47 billion in 1984. It is the fifth largest world oil producer and third largest exporter. Domestically, oil revenues provide about 90 percent of foreign exchange, 25 percent of the GDP, and 70 percent of the annual budget. Approximately three-fourths of the petroleum output comes from the Maracaibo basin, and most of the remainder comes from the Orinoco basin. Venezuela has additional, but as yet largely untapped reserves of highly viscous oil in the Orinoco Tar Belt. Development of these reserves has been placed on hold, pending revival of world market demand. Venezuelan industry is in transition from small, labor intensive units engaged in the production of intermediate and consumer goods to large enterprises producing heavy and capital goods. This process has been fueled by a strategy of plowing oil revenues into industrial development and diversification in order to create key supplementary sources of revenue. Large scale industries established or expanded with oil dollars in the past decade include steel, aluminum, alumina, petrochemicals, iron-ore mining, and hydroelectric power. Agriculture contributes 6 percent of the GDP and its share of export earnings is negligible. Although, Venezuela is a net food importer, it has reduced its external dependency significantly since 1983. 25X1

Economy at a Glance

Venezuela has a population of nearly 18 million. In 1985 the literacy rate was 85 percent, up approximately 10 percent from 1982. The country has universal, free, and compulsory primary education. As far as basic infrastructure is concerned, Venezuela has 78,000 kilometers of highways, approximately a fourth of which are paved. Venezuela also has 7,000 kilometers of usable inland waterways; the Orinoco River and Lake Maracaibo accept oceangoing vessels. Moreover, Venezuela has 6 major ports and 17 minor ports. In addition, the country has nearly 240 usable airfields, approximately 100 of which have permanent-surfaced runways. Venezuela has a modern and expanding telecommunications system and extensive radio relay facilities. Venezuela is the fourth most urbanized nation in South America (after Uruguay, Chile, and Argentina); nearly 70 percent of the population live in urban communities with more than 2,500 inhabitants. Among non-oil minerals, iron-ore is most actively exploited. Iron reserves are estimated at 2 billion tons of high-grade ore and 7.5 million tons of low-grade ore. Production of coal, gold, and diamonds has been declining. Other minerals known to exist, but not yet mined, include manganese, mercury, nickel,

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magnesite, cobalt, and mica. Proven petroleum reserves are officially placed at 30 billion barrels of conventional crude, plus the Orinoco Tar Belt reserves, which are said to exceed 1.2 trillion barrels. 25X1

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