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The Director of Central Intelligence
Washington, D.C. 20505

National Intelligence Council

C/NIC CHRONO
NIC #02873-84
15 May 1984

MEMORANDUM FOR: Director of Central Intelligence
Deputy Director of Central Intelligence

VIA: Chairman, National Intelligence Council *g*

FROM: Maurice C. Ernst
National Intelligence Officer for Economics

SUBJECT: International Debt Problem

1. The attached memorandum summarizes the discussion at the Monday SIG-IEP meeting on the international debt problem. There is a broad consensus that aspects of the US strategy will have to be reexamined after the Economic Summit. As I indicated in my memo of 26 April 1984, I believe it will be essential to find ways of easing the pressure on the IMF, through supplementary financing mechanisms and probably also by easing some of the current conditionality requirements.

2. In some ways the LDC debt problem is in a stage of transition from helping LDC debtors make ends meet to finding politically acceptable ways of enabling them to resume economic growth. Some of the debtors, notably Mexico, have all but eliminated payments arrears and improved their foreign exchange position, mostly through import cuts, to the point that they could begin to finance a moderate rate of increase in imports, and consequently in economic growth. Yet these economies, including the Mexican economy, are apparently continuing to decline well below what their governments and the IMF had anticipated. The reason appears to be that the public sector is continuing to contract, largely to meet IMF-imposed conditions, while the private sector is not making up the slack, so that effective demand is continuing to decline. This situation may become characteristic of more and more countries in the course of 1984. If it continues for long, political pressure to stimulate economic recovery by once again increasing government expenditures may become irresistible in the debtor countries. Public sector lending growth in turn would quickly come in conflict with IMF guidelines and with US Government objectives. It would require some difficult policy choices.



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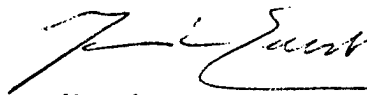
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3. These changing problems have implications for CIA and Intelligence Community analysis. Although there will be a continuing heavy demand for detailed analysis of LDC debt and balance of payments conditions and prospects, it will become increasingly important to address the following questions:

- o What are the political pressures and requirements for economic recovery in the major debt-ridden LDCs?
- o By what means could such recoveries be achieved?
- o What economic policy trade-offs might be necessary in the debtor countries?

4. Addressing these questions will require an even closer examination of the factors that drive domestic income, expenditures, and production in the debtor countries, as well as imports and exports, and at the evolving politics of the debt problem in each country.



Maurice C. Ernst

Attachment:
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