Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Directorate of
Intelligence

~~Secret~~

25X1

File Copy

Do not remove

6 art.
36 briefs

International Economic & Energy Weekly

25X1

20 December 1985

~~Secret~~

DI IEEW 85-050
20 December 1985

Copy 685

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Page Denied

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Secret
Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7 [redacted] 25X1

International Economic & Energy Weekly [redacted] 25X1

20 December 1985

[redacted] 25X1

Comments and queries regarding this publication are welcome. They may be directed to [redacted] *Directorate of Intelligence,* [redacted] 25X1 25X1

Secret
DI IEEW 85-050
20 December 1985

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

25X1

International Economic & Energy Weekly 25X1

Synopsis

1 **Perspective—Free Trade Agreements With the United States** 25X1

The US' offer to discuss free trade agreements (FTAs) with foreign countries has met with mixed response. Interest in FTAs would probably rise if progress on the new GATT round stalls. 25X1

3 25X6 X1

25X1

7 **South Korea: Ready To Deal on Trade Issues?** 25X1

Seoul has signaled its willingness to settle specific trade disputes now on the table—access to the Korean insurance market and protection of intellectual property rights—by offering concessions during bilateral trade discussions last week. Even so, we expect that concrete results in these areas and progress on other outstanding trade issues will be slow. 25X1

13 **Argentina: Trade Policy and Prospects** 25X1

Argentina's ability to export its way out of the debt crisis has been hampered by its inconsistent trade policies. We judge that President Alfonsin will continue to subordinate trade expansion to other economic and political policy goals over the near term. 25X1

19 **Intra-African Smuggling: A Pervasive Phenomenon** 25X1

Smuggling is rampant in Sub-Saharan Africa—equaling, or exceeding, the value of recorded nonoil trade according to our estimates—and involves a wide variety of goods. While usually viewed by African governments as undesirable, smuggling, nonetheless, has benefits to the extent that it provides a way for Sub-Saharan economies to overcome the difficulties caused by inefficient government policies. 25X1

DI IEEW 85-050
20 December 1985

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

[redacted] 25X1

International Economic & Energy Weekly [redacted] 25X1

20 December 1985

Perspective

Free Trade Agreements With the United States [redacted] 25X1

The US offer to discuss free trade agreements (FTAs) with foreign countries has met with mixed response. Earlier this year the United States and Israel signed such an agreement, and Canada has officially notified Washington of its interest in discussing freer trade. Elsewhere, however, interest has been muted. [redacted] 25X1

Interest in bilateral free trade agreements has been stimulated by lack of progress in trade liberalization through the multilateral trading structure. Supporters of FTAs believe they provide several advantages: they liberalize trade; demonstrate a commitment to, and the advantages of, market-oriented policies; can address issues specific to the bilateral trade relationship; and guarantee long-term access to a market. Opponents claim FTAs will lead to a lopsided system of discriminatory agreements that exclude many LDCs, alienate nonparticipants, are politically motivated, and have no clear advantages. For an FTA to be compatible with the GATT it must cover substantially all trade between the countries, be implemented within a reasonable time, and not increase barriers to nonsignatories. Many countries say they are reluctant to deviate from their commitment to the multilateral framework. [redacted] 25X1

Except for Canada and Israel, few countries have expressed interest in FTAs, although the possibility of FTAs has been raised with the six nations of ASEAN and Saudi Arabia. At present none of the seven countries has requested negotiations. [redacted] 25X1

The restrained response is due to a variety of factors:

- Singapore is promoting an ASEAN-US FTA, but response from other ASEAN nations has been cool. Their comments indicate that they want the United States to take the initiative and demonstrate evidence of concrete benefit to their economies. They are suspicious of Singapore's motives, believing it would be the largest beneficiary due to its already open economy. In addition, an FTA would permit open access to their markets for the United States. They would prefer the agreement to be development-oriented along the lines of the Caribbean Basin Initiative. If Singapore cannot get ASEAN support, it may initiate a bilateral agreement on its own.

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

- Few other countries have expressed a serious interest in an FTA which meets all the US and GATT requirements. Saudi Arabia would be interested primarily in protecting its access to the US market for petroleum exports; Uruguayan officials have expressed interest in an agreement for the smaller Latin countries; and a Taiwanese economics minister has said he favors an FTA as a long-term device for narrowing the trade gap with the United States. [redacted] 25X1

Future initiation of FTAs will probably be slow as attention is focused on the preparatory phase of the new GATT round scheduled to begin in September 1986. Interest in FTAs would probably rise if progress on the new round stalls. LDCs are afforded special treatment in the GATT system and have indicated they expect the same in bilateral agreements. They are interested in guaranteed access to the US market, but they want the United States to make most of the concessions. They are unsure of the impact of an FTA, with many believing their national sovereignty would be threatened. Nonetheless, a lack of alternate forums to negotiate trade liberalization and US-market access might encourage them to consider it. [redacted] 25X1

[redacted] 25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

25X1

25X1

Page Denied

25X1

Next 4 Page(s) In Document Denied

25X1

25X1

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

South Korea: Ready To Deal on Trade Issues? [redacted]

25X1

After four months of fanning the public outcries against US pressure for market-opening measures, Seoul signaled its willingness to settle specific trade disputes now on the table—access to the Korean insurance market and protection of intellectual property rights—by offering concessions during bilateral trade discussions last week. Even so, we expect concrete results in these areas, and progress on other outstanding trade issues will be slow. Seoul would probably find it easiest to deal with additional US initiatives aimed at the exports of large South Korean conglomerates—the government already favors a policy to limit their power. The government would likely react strongly, however, to measures targeting such politically sensitive and beleaguered sectors as agriculture, textiles, footwear, and small- and medium-sized industries. [redacted]

Section 301 of the Trade Act of 1974

Section 301 of the Trade Act of 1974 authorizes the President to take action against foreign trade practices that violate international trade agreements or burden or restrict US commerce in an unjustifiable, unreasonable, or discriminatory fashion. Section 301 is intended to cover not only trade in products (goods) but also foreign practices affecting services, investment, and intellectual property rights. Section 301 actions may be initiated by industries feeling the pinch of allegedly unfair trade practices or by the President of the United States—a so-called self-initiated 301. [redacted] 25X1

Under Section 301, the President has the authority to take all appropriate and feasible actions to obtain the elimination of unfair trade practices. Specifically, he may impose duties, fees or restrictions on products and services of the foreign country involved. These restrictions do not necessarily have to be applied to, or related to, the products and services that are the subject of the 301 complaint. The President may also deny licenses issued by federal regulatory agencies to foreign service suppliers. The degree and duration of these actions is up to the President, but he will not retaliate against a country unless the 301 case adequately demonstrates that these policies are actually harming US export interests. [redacted]

25X1

25X6

25X6

25X1

Seoul Makes a First Step

In an effort to quickly settle US Government–initiated 301 actions, Seoul made some concessions on copyright and trademark protection during bilateral trade negotiations last week—discussion focused on intellectual property rights and access to the insurance market for US firms. The order to compromise came from the top, [redacted]

25X1

Despite the glimmer of hope offered by Seoul's softer stance on these longstanding trade issues, nettlesome problems remain, particularly in patent and computer software protection and the fire and life insurance areas. We believe concrete results will come only after continued hard-nosed negotiations on issues still on the docket and pressure to implement reforms already promised. Seoul could well revive its traditional stalling tactics or retract proposals made if it believes Washington remains dissatisfied with what it considers goodwill gestures. South Korea may also calculate that US attention to trade issues will decline once the 1986 Congressional elections are over and that delaying tactics will enable South Korea to wait out the furor. [redacted] 25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Moreover, Seoul's earlier efforts to foment anti-US reaction on trade issues may have reduced its room for further compromise. Violent student demonstrations have increasingly featured anti-US themes criticizing South Korean dependence on the US economy and Washington's call for market opening. If Chun reverses his hard stance now in favor of compromise, radical students, and perhaps some of his more moderate critics, will accuse him of giving in to US pressure.

In sum, we do not rule out the possibility that Seoul might make one or two bold gestures that could quickly close the books on insurance and intellectual property issues. We believe it is more likely, however, that South Korean negotiators will take an incremental approach, carefully weighing Washington's response at each turn, in the hope of giving up as little as possible. Senior economic officials in Seoul apparently still believe that, because of its "special" relationship with the United States, South Korea may be able to avoid stern US trade actions.

Seoul's Likely Response to Additional Trade Measures

In our view, South Korea is bracing for additional US trade action, partly because it expects its response on the insurance and intellectual property rights cases may fall short of US demands. On the basis of South Korea's track record, we judge there is likely to be a range of reactions to new moves by Washington. In some cases, bureaucratic realities will shape the speed and response to selected US trade actions. In others, political factors will weigh more heavily.

Straining the Bureaucratic Machinery. Consensus among Seoul's policymakers—a key to resolving current trade difficulties—is a time-consuming process involving entrenched opponents of market opening and the numerically weaker, proliberalization members of Chun's economic policy team. The differences between these two groups would make further, quick compromise difficult if the United States pressed for speedy resolution of these two cases. Chun could force acceptance of his economic advisers' views, but such snap concessions could later open him to attack from opponents of reform.

25X1

To be sure, the limited scope of the 301 cases on the table restricts the number of interested parties. But the few players involved—mainly the large conglomerates—have important financial stakes. The conglomerates not only profit from the lack of protection afforded foreign patents and copyrights under Korean law, but are also the owners of many of the insurance companies. Moreover, their insurance operations provide a ready source of loans with "no questions asked" for cash-strapped subsidiaries. Their past behavior suggests they will press Seoul to engage in foot-dragging in response to US demands. The government cannot afford to ignore their problems, since it is committed to covering the bad debts of the corporate sector to maintain the solvency of the commercial banks.

25X1

25X1

Additional US 301 actions would also strain Seoul's policymaking resources, as the few qualified personnel divide their attention among new challenges. Moreover, Seoul perceives its efforts to resolve cases already on the table—no matter how modest—as sincere gestures, and there could well be a backlash against the United States if Washington takes additional trade actions while negotiations are under way. More 301s would also reinforce the South Korean perception of being unfairly singled out for punishment.

25X1

25X1

Targeting Exports Could Hit Political Nerves. Seoul probably calculates that sanctions against specific South Korean exports to the United States would not inflict serious economic pain.[1] We believe, therefore, that Seoul would shape its negotiating stance largely in response to the domestic political reaction—and consequent costs to the government. Retaliatory measures that target vulnerable sectors, while capturing Seoul's attention,

25X1

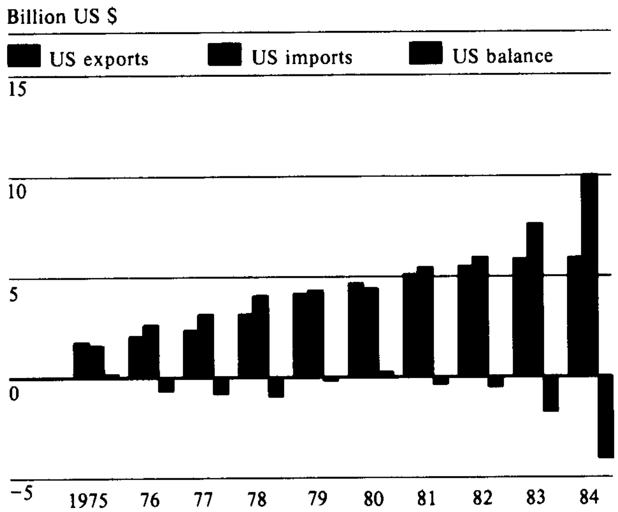
[1] The GATT limits punitive actions by one country to the amount of injury it has suffered because of a partner's trade practices. Calculating the loss to US interests from South Korea's closed insurance market and lax intellectual property rights enforcement is at best an art.

25X1

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

US-South Korean Trade, 1975-84



307673 12-85

would risk renewed sharp press reaction as well as anti-US and anti-Chun attacks from radical students. The sensitive sectors include:

- Agricultural products. Although agricultural goods account for only 1.5 percent of US purchases from South Korea, the rural sector remains a pivotal political constituency. An apparent failure by Chun to protect the interests of "poor farmers" would open him to widespread criticism, even from the urban population.

- Small- and medium-sized firms. South Koreans would view actions against products of these firms as cases of the strong picking on the weak. A replay of the visceral South Korean response to the large duties imposed on photo album producers—generally very small, labor-intensive firms—would be likely. Such US moves would also erode sympathy for Washington among proliberalizers, who want to encourage small business growth and stem industrial concentration in the large conglomerates over the long run. 25X1

Even more difficult for Seoul to deal with would be trade measures aimed at the textile industry. Beyond the importance of textiles as a key export—25 percent of South Korea's exports to the United States last year—the industry's health could play a crucial role in domestic political stability and in setting the overall tone of future trade negotiations:

- Restrictions on textile goods would hit hardest in provincial manufacturing centers that are already economically depressed and where opposition to Chun's economic agenda runs particularly deep. These areas, like Seoul, have been the scene of recent anti-US protest actions.

- Smaller textile manufacturers, who subcontract from the dominant firms, would disproportionately shoulder the burden of cutbacks. 25X1

The depth of South Korean reaction to textile-related US measures could grow considerably if there was a general perception that the Jenkins Bill—or similar bills—would become law. According to the US Consulate in Pusan, the passage of a Jenkins-like bill would cut an estimated $150 million from Pusan area textile sales and force the firing of 10,000 to 15,000 workers. 25X1 25X1

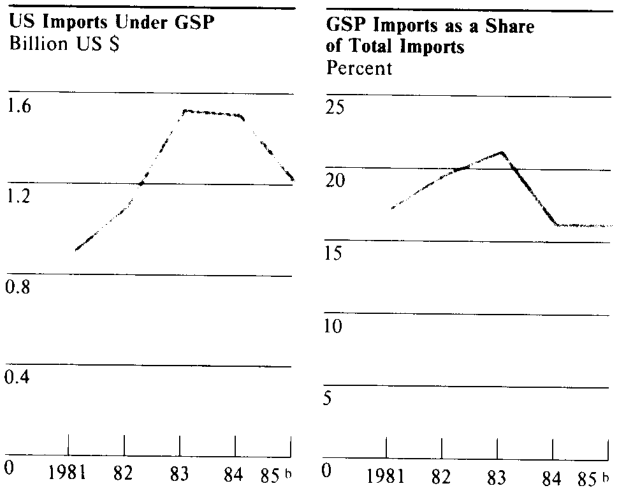
Trade actions against these politically sensitive industries would encourage Seoul to make good on its threats to retaliate by switching to other sources for major imported items. Agricultural products—which accounted for $1.5 billion in US exports to South Korea in 1984—would be one obvious category; energy resources would be another. So far, we have seen no evidence that South Korea plans to carry through with these threats, but it could do so—though not easily—by shifting substantial shares of grain and coal imports to other countries, such as Canada, Australia, and, even China. 25X1

Conglomerates—Big Bull's-Eye

We would expect more flexibility in Seoul's bargaining positions and continued commitment to

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

US Imports of South Korean Goods Under GSP,[a] 1981-85



[a] Generalized.
[b] Data through September 1985.

307674 12-85

implementing its reform program if action directed at Korean goods took the form of a "surgical strike" against selected exports of the conglomerates. Since he came to power in 1980, Chun has allowed his economic team to limit the growth and political clout of the large firms. The current economic slowdown, however, has forced Seoul to partially abandon much of that policy in the hope that feeding the conglomerates' appetite for growth will spark a broad recovery. Chun could find it convenient to agree to actions against the conglomerates as a way to show them that the favorable treatment they now enjoy is only temporary while saddling the United States with the blame for reforms.

Most South Koreans recognize that some practices by the major conglomerates—such as violation of intellectual property rights—are indefensible. Trade actions targeted only at those who are guilty is unlikely to generate enmity toward Washington—or Chun. Finally, focusing on such exports could lessen conglomerate pressure on the government to protect insurance markets, since the large firms would be likely to suffer most from retaliatory sanctions. 25X1

Targeting higher technology, capital-intensive and higher value-added exports that depend on the US market for their success will probably have the best chance of convincing conglomerates to ease pressure on Seoul and endorse new regimes for insurance and intellectual property rights. Pressure points that would make the conglomerates most likely to sign up include:

- ***Automobiles.*** Hyundai will inaugurate its flow of South Korean autos to the crucial US market in January, when the low-priced "Pony Excel" goes on sale. Korean auto firms are predicating their success in the US market primarily on price competitiveness, and any tariff that closes the price gap would dim prospects. The threat of automobile trade barriers would send tremors far beyond Hyundai—Daewoo and Kia already are preparing for the US market, and Samsung, which has important insurance holdings, hopes to gain government approval to produce cars as well. 25X1

- ***Microelectronics.*** Samsung, Lucky Goldstar, Daewoo, and Hyundai have large investments in the semiconductor and personal computer businesses. Their results have been unprofitable so far, but they see success in the long run. These firms have committed their prestige as well as capital to high-technology ventures and will want to avoid sustaining losses caused by trade friction. 25X1

Barriers to exports of less visible products produced by the large firms—such as videocassette recorders sold under US brand names—could also cause them to agree to reforms. Their responsiveness will depend on their ability to pass on the pain of sanctions to subcontractors who supply parts or other services. 25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Outlook

In general, we believe Chun and his advisers are committed in principle to economic reform because they are concerned about their long-term access to US markets and technology and worried about the danger of wholesale barriers to Korea's exports. Legislation that would cut back exports of key goods, such as textiles, and South Korea's possible loss of the benefits from the Generalized System of Preferences—the GSP renewal process now in progress—are an important part of Seoul's calculations. Withdrawal of even some GSP benefits would seriously impair the cost competitiveness of many South Korean export goods. It would hit small firms hard—limiting their export growth—although it would not sound a death knell for any key South Korean industries. [redacted] 25X1

Moreover, Chun may have difficulty containing damage to his domestic political position if trade issues become a rallying point for his opponents. Further complicating his position is the likelihood that US restrictions on Korean exports will aggravate the current economic slowdown—which in turn could produce higher unemployment and the possibility of political instability. We expect him to use the prospect of future harm to South Korea's exports to strengthen his hand in pressing for economic reforms as long as the domestic political cost of that response to Washington remains manageable. [redacted] 25X1

[redacted] 25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Argentina: Trade Policy and Prospects

25X1

Argentina's ability to export its way out of the debt crisis has been hampered by its inconsistent trade policies. Buenos Aires has boosted its trade surplus sharply over the past three years but only at the cost of restraining imports. Export growth has been plagued by erratic policies, an overvalued currency, and low world agricultural prices. President Alfonsin has announced his desire to boost trade, but has made little progress toward stimulating exports and reducing import restrictions. We judge that he will continue to subordinate trade expansion to other economic and political policy goals over the near term. As a result, Argentina will need to borrow at least $2 billion next year to finance its current account deficit.

Argentina: Current Account Balance — *Billion US $*

	1982	1983	1984	1985 [a]	1986 [a]
Trade balance	2.7	3.7	4.0	3.5	3.4
Exports, f.o.b	7.6	7.8	8.1	7.7	7.7
Imports, f.o.b	4.9	4.1	4.1	4.2	4.3
Service balance	−4.8	−6.1	−6.5	−5.4	−5.5
Interest	−5.3	−5.4	−5.5	−4.3	−4.4
Other	0.5	−0.7	−1.0	−1.1	−1.1
Current account balance	**−2.1**	**−2.4**	**−2.5**	**−1.9**	**−2.1**

[a] Projected.

25X1

25X1

Trade Policy and Performance Since the Debt Crisis

With the advent of the debt crisis and the falloff in bank lending in 1982, major Latin American debtors attempted to improve their financial position by increasing their merchandise trade surpluses. Argentine trade policy between 1982 and 1984 focused on import restriction. The Secretariat of Commerce prohibited the importation of many products considered to be luxury items or that could be produced internally, and subjected others to time-consuming and costly licensing procedures.

The government's efforts at export promotion suffered from the lack of a permanent, predictable trade policy. Buenos Aires erratically established, revised, or eliminated export incentives, while fluctuating export tariffs and a consistently overvalued currency hampered exporters' ability to plan ahead and compete. External factors—such as declining international agricultural prices as well as EC protectionist policies and export subsidies—also stymied Buenos Aires's export push.

Despite these difficulties, Argentina's trade surplus improved 74 percent to $4.0 billion during 1982-84. Most of the gain was due to import cuts, however. Imports dropped 23 percent while exports increased only 7 percent over the period. 25X1

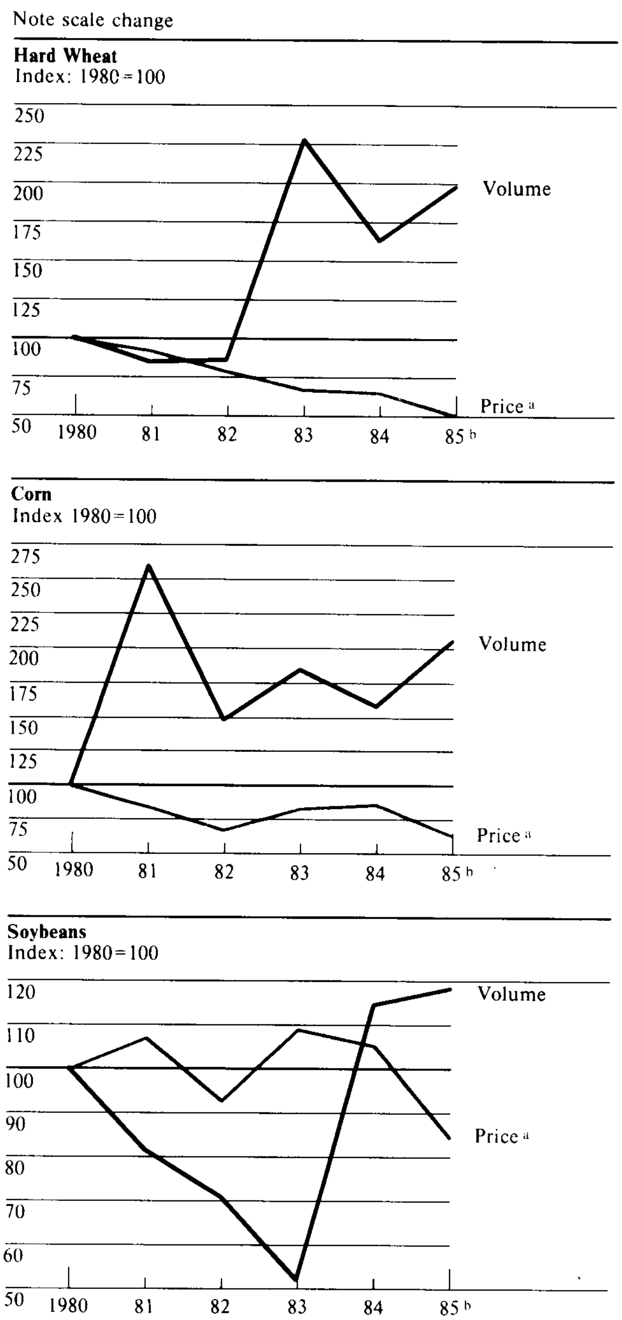
In 1985, Buenos Aires began a more concerted effort to stimulate exports by removing export tariffs for most manufactured products, cutting the tariff on wheat exports from 26.5 to 15 percent, and altering the value-added tax system. Embassy reporting indicates, however, that the government's commitment to export expansion has been limited. 25X1 The austral, the new currency unit adopted in June, is consistently 10 to 20 percent overvalued, hindering exporters' ability to compete on the international market. In addition, the government has yet to enact legislation to implement the 1984 Export Promotion Law, which would spur exports through tax rebates, deductions, and credits. Meanwhile, on the import side, Buenos Aires levied a 10-percent

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Argentina: Prices and Volumes of Leading Exports, 1980-85



[a] US f.o.b. price Buenos Aires $ per metric ton.
[b] Forecast.

307666 12-85

Argentina: Composition of Trade, 1984 *Billion US $*

Exports, f.o.b.	**8.1**
Grain and oilseeds	3.2
Livestock, animal products	0.4
Other agricultural products, including fats and oils	1.2
Manufactured goods and other	1.9
Minerals and chemicals	0.7
Textiles, leather	0.7
Imports, c.i.f.	**4.5**
Capital goods	0.8
Consumer goods	0.2
Intermediate goods	3.5
Fuel and lubricants	0.5
Chemical products	0.9
Machinery	0.6
Metallurgical products	0.5
Plastics	0.3
Other	0.7

25X1

surcharge, and other restrictions remain in place, despite promises to the IMF to liberalize imports.

25X1

We are projecting a 5-percent drop in export revenue this year—largely the result of declining prices for agricultural goods. While the press reports that Buenos Aires forecasts a 19-percent increase in industrial exports during 1985, official statistics indicate a 4-percent drop during the first trimester; we have seen no evidence to support more than a modest increase in manufactures shipments since summer. Continued restrictions should, in our view, keep import levels in rough parity with 1984.

25X1

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

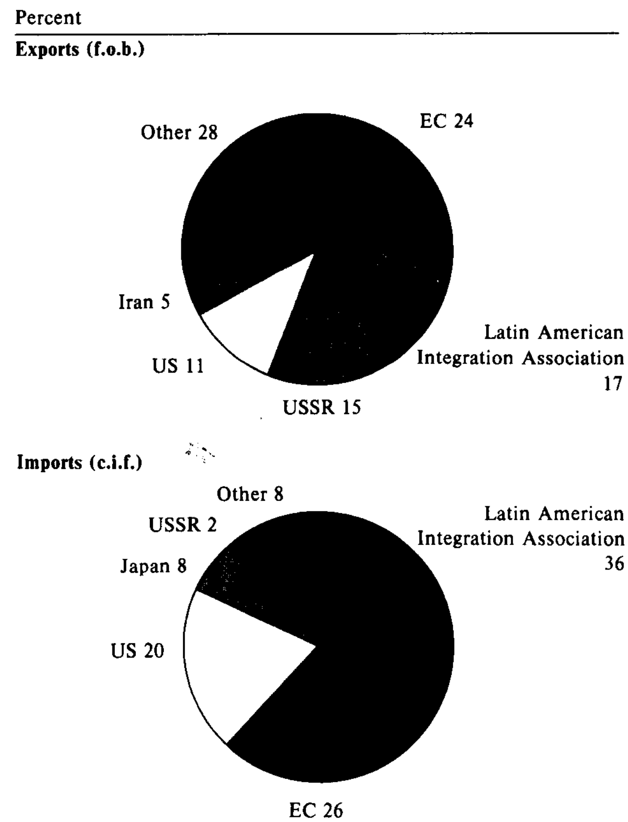
Shifts in the Direction of Trade

The most important single importer of Argentine goods is the Soviet Union. The USSR purchased $1.2 billion, primarily agricultural goods, from Argentina last year, accounting for 15 percent of Buenos Aires's total exports. This was down from $1.8 billion, or 23 percent of the total, in 1983—in our view, because of an improved Soviet harvest and Moscow's growing displeasure over its lopsided trading relationship with Argentina. The US Embassy reports that Buenos Aires has begun to respond to Soviet pressure to increase purchases by awarding the USSR contracts for highway construction and railroad electrification projects. Alfonsin, however, has spurned major contracts—such as Moscow's proposals to modernize the port of Bahia Blanca and sell arms to the Argentine military—largely, in our view, because he fears that such moves could enhance Moscow's political influence in Argentina and lead to dependence on Soviet technology.

The EC is the largest group buyer of Argentine exports, purchasing oilseeds to supply its crushing industry. Until recently, Buenos Aires's fastest growing trading partner was Iran; it imported $430 million worth of Argentine goods last year, up 221 percent since 1982. The press reports, however, that Tehran's displeasure over its trade imbalance with Buenos Aires and Argentina's plans to sell Pucara aircraft to Iraq have prompted Iran to cancel further grain purchases from Argentina. We believe, however, that the cancellation is largely a bargaining ploy which could readily be reversed should Argentina agree to additional purchases of Iranian goods; an exchange of trade delegations is already underway.

The United States is the single largest source of imports for Argentina, although their dollar value—on a c.i.f. basis—declined 25 percent to $884 million between 1982 and 1984. US exports consist chiefly of chemicals, machinery and transport equipment, and other manufactured products. Other major partners include Brazil, West Germany, and Japan.

Argentina: Direction of Trade, 1984



25X1

25X1

307667 12-85

Trade Policy in the Future

25X1

While the Argentine economy would greatly benefit from trade expansion, there are short-term drawbacks to trade-promoting policies. Lowering export taxes—which currently account for 20 percent of government revenues—would immediately reduce Buenos Aires's cash flow, even though in the long run this might be offset by increased export volume. Moreover, a market-level exchange rate 25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

would increase inflationary pressures. Import liberalization would also narrow the trade surplus and hurt inefficient local industries, thereby raising unemployment in the short term.

We believe that Alfonsin's current strategies will inhibit aggressive trade-promoting policies. The President's major economic and political goals, in our view, are to keep inflation low and reduce the fiscal deficit so that the public continues to perceive that his austerity program—the success of which accounted for much of his party's good showing in recent Congressional elections—is working well. His secondary aims include economic growth and the repayment of interest on the foreign debt. Given Alfonsin's emphasis on quick (one year or less) results and his probable reluctance to court labor unrest by tolerating large increases in joblessness, we doubt that the government will take the risky short-term steps needed to spur a long-term export-led economic recovery. Thus, we expect Buenos Aires to continue to overvalue the austral, vary export taxes according to the extent of shortfalls in the federal budget, and retain numerous import restrictions.

Alfonsin, however, is capable of bold changes in economic policy, as evidenced by his sudden imposition of the "austral plan" last June. We believe there is roughly a 1-in-3 chance that the President may, over the next few months, introduce some of the structural reforms required for the Argentine economy's long-term health. The first indication of such a shift would probably be the replacement of advocates of a strong public-sector role, such as Energy Secretary Storani and Central Bank head Concepcion, with technocrats in Finance Minister Sourrouille's mold. Followup indicators would include greater efforts to lure private investors into public-sector-dominated industries, such as oil and telecommunications, sales of major state enterprises to the private sector, passage of enabling legislation for the Export Promotion Law, and the permanent lowering of export taxes.

Outlook

We do not expect exports to increase appreciably during 1986. Much of the success Argentina may experience in expanding industrial exports next year will, in our view, be counteracted by losses in agricultural income. Tight credit policies combined with the flooding of 6 million hectares of farmland this fall will keep agricultural production under last year's levels, and commodity prices are unlikely to rise sufficiently to compensate for this loss. Imports may increase by 2 percent should Alfonsin succeed in boosting 1986 GDP.

25X1

25X1

Prospects for increased trade surpluses are somewhat more favorable over the long term. A slow but steady increase in state and foreign investment in the energy sector should enable Argentina to boost its oil and natural gas production significantly over the next five years. According to press reports, Argentina has estimated gas reserves of 680 billion cubic meters and is considering constructing pipelines to transport its gas to Chile and Brazil. Most other industries are operating at low-capacity utilization rates, which would enable them to boost production for export without additional capital investment, according to a recent World Bank study. Nonetheless, much of Argentine industry is ill equipped to compete on the international market without substantial restructuring.

25X1

25X1

The outlook for expanded agricultural exports is good, although we view Buenos Aires's publicly stated goal of boosting grain and oilseed production to 60 million metric tons by 1990 from 41 million tons last year as somewhat optimistic. this goal is attainable if Buenos Aires modernizes its logistic network and increases incentives and supports to farmers growing export crops. The government has taken some initial steps, such as accepting bids on the Bahia Blanca port modernization project and reducing export tariffs. Moreover, a US Department of Agriculture official maintains that the likely

25X1

25X1

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

passage of a land tax as a partial substitute for export taxes will provide landowners with incentives to spur production and enable Buenos Aires to further lower the export tax. However, the erratic nature of government policy, combined with declining terms of trade and heated competition in the international grain market, leads us to expect a more limited increase above current production levels throughout the remainder of the decade. 25X1

25X1

Implications for the United States

Argentina's limited commitment to export stimulation will, in our view, contribute to a continuing need for new money to service its $50 billion debt. This will require continued involvement on the part of the US Government and banking community to assure that Buenos Aires does not again incur large-scale interest arrearages. In addition, although likely to make a few cosmetic changes to satisfy IMF requirements, Buenos Aires will probably not return to a policy of liberalizing imports in the foreseeable future. Thus, US exports to Argentina are unlikely to approach pre-1982 levels over the next two to three years. Buenos Aires will continue to compete with the United States in international agricultural markets, especially in wheat and oilseeds. Finally, some of the limited export incentives Buenos Aires gives domestic producers—such as tax breaks for oilseed crushers—probably will violate the GATT, thereby straining commercial relations with the United States. 25X1

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Intra-African Smuggling: A Pervasive Phenomenon [redacted] 25X1

Smuggling is rampant in Sub-Saharan Africa [1]—equaling or exceeding the value of recorded nonoil trade, according to our estimates—and involves a wide variety of goods. This large-scale illegal trade is the result of overvalued exchange rates, protectionist tariffs and quotas, and low government procurement prices. Smuggling is usually viewed by African governments as undesirable, because the erosion of the "official" trade base reduces foreign exchange earnings and government revenue, and fosters corruption. Nonetheless, smuggling has benefits to the extent that it provides a way for Sub-Saharan economies to overcome the difficulties caused by inefficient government policies. [redacted]

Estimating Illegal Trade

Smuggling among Sub-Saharan African countries exists on a large scale and involves a wide variety of commodities, including livestock, coffee, cocoa, maize, cooking oil, narcotics, and consumer products ranging from soap to automobiles and other luxury items. While it is not possible to arrive at firm estimates of the value of unrecorded trade, the sketchy data available indicate that it is as big or bigger than the estimated $5 billion in recorded nonoil intra-African trade:

- Private studies estimate that smuggling from Benin to its neighbors amounted to 10 billion CFA francs (more than $35 million) for 1971-72, nearly half the size of recorded exports.
- Cocoa smuggling in Ghana in 1982 amounted to nearly three times recorded cocoa exports, according to a private study.
- [redacted] total cattle exports of Mali in 1970 were 230 percent of recorded exports, and that actual exports from Togo to Ghana were 14 times recorded exports.

[1] Excluding South Africa. [redacted]

Selected Examples of Sub-Saharan African Smuggling

Year	Countries Involved	Comments
1984	Senegal	An estimated 40 percent of the peanut harvest (260,000 metric tons) was smuggled out of Senegal.
1983	Cameroon and Nigeria	140,000 tons of rice were smuggled from Cameroon to Nigeria.
1983	Niger and Nigeria	Smuggled exports of millet totaled well over 140,000 tons.
Early 1980s	Burkina, Mali, and Niger	Cattle smuggled into Niger from Burkina and Mali vary from 30 to 40 percent of recorded Nigerien cattle imports depending on the smuggling route.
1980-81	Mali	Illegal exports of cattle, sheep, and goats totaled 200 to 300 percent of recorded exports.
1975-80	Uganda	Smuggled coffee exports averaged 20 to 50 percent of recorded coffee exports.
1975	Chad	Unofficial cattle exports estimated at 240,000 head; 160,000 to Nigeria and the rest to Cameroon and the Central African Republic.

25X1

[redacted] 25X1

- The Central Bank of Burkina estimates that between 1977 and 1979 smuggling totaled between 75 and 125 percent of recorded trade. [redacted] 25X1

Causes of Smuggling

Most smuggling in Africa is caused by a combination of large price differentials between neighboring countries and trade barriers, such as tariffs and import quotas. These differentials and trade barriers are in turn the result of inappropriate government policies: 25X1

- ***Overvalued exchange rates.*** In African countries such as Nigeria and Tanzania, inflationary mone-

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

tary and fiscal policies and the failure of the authorities to adjust exchange rates have created overvalued currencies. These overvaluations lower the domestic-currency price of exports and encourage exporters to turn to smuggling to obtain higher prices for their products. Overvalued exchange rates also increase the demand for imports, requiring the imposition of exchange controls or import quotas to prevent balance-of-payments difficulties. Consumers or producers who are unable to obtain scarce foreign exchange or imported goods will turn to smuggling to satisfy their needs.

- ***Inward-looking development strategies.*** Many African states have adopted development strategies that involve the creation of import-substituting industries that are often inefficient producers of high-cost, lower quality goods. As a result, these industries require a high degree of protection, raising the domestic price level, increasing the demand for higher quality imports, and creating fertile ground for smuggling.

- ***Poor pricing policies.*** Low prices paid by government purchasing agencies to domestic producers—often part of a strategy to keep urban food prices low to prevent unrest in major population centers—provide an incentive to channel production into smuggling where producers can obtain higher prices. In Sierra Leone, rice can be sold on the black market for over three times the official buying price.

Although smuggling is frequently difficult to control in remote border areas of these LDCs, a pervasive climate of official corruption—at times even tolerated by the regime—is a contributing factor.

Costs and Benefits of Smuggling

African governments officially disapprove of smuggling because it erodes the official trade base, with the consequent loss of official foreign exchange earnings and reductions in government revenue from tariffs and taxes. This view, however, implies that smuggling is simply a diversion of trade from official to unofficial channels.[2] This is not always true, since in many instances the alternative to smuggling is not increased official exports but decreased domestic production of export goods, given the inefficient government policies in effect. Therefore, smuggling would not result in a loss of government revenue and foreign exchange earnings, because in the absence of smuggling the export goods may not have been produced anyway.

25X1

Moreover, we believe smuggling has beneficial aspects, because it allows African economies to circumvent the effects of inappropriate government policies and function more efficiently by:

- Increasing the availability of goods, since many imported goods are unavailable at controlled or overvalued exchange rates.
- Stimulating the economy by encouraging increased production of export goods.
- Developing parallel markets that effectively provide a de facto exchange rate devaluation.
- Improving income distribution by raising the incomes of agricultural exporters, who are usually small-scale traders.

Smuggling therefore provides a "second-best" solution to the problems caused by inappropriate government policies. In addition, the ease with which smuggling and parallel markets arise demonstrates that markets can function at a reasonable level of efficiency in Sub-Saharan Africa, despite the rhetoric of many African leaders. 25X1

Government Reactions

25X1

In response to widespread smuggling, many countries, such as Nigeria and Tanzania, have allocated funds to control smuggling more effectively. However, efforts to reduce smuggling are likely to have limited success. Few African governments have the resources of money and manpower needed to deal

[2] For example, goods may be smuggled through unofficial channels to avoid payment of taxes. 25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

with smuggling. Moreover, in countries such as Nigeria and Sierra Leone smuggling has become ingrained in every level of society, ranging from the farmer to government officials, and effective anti-smuggling efforts could lead to a loss of domestic political support. 25X1

In addition, it is possible that Sub-Saharan African governments, facing increasing economic difficulties and uncertain domestic support, could view a combination of modest economic reforms and a more tolerant attitude toward smuggling as an alternative to adopting radical measures and risking a surge in domestic unrest. This type of "benevolent connivance" would increase economic efficiency without the need to cope with the political, economic, and social problems that would result from an all-out campaign to control smuggling or from the elimination of the inefficient government policies that lead to smuggling. 25X1

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Jamaica: Accelerating Economic Slide

25X1

Unless Jamaica substantially improves its track record with the IMF and steps up diversification, its economy—hobbled largely by sagging bauxite/alumina production—probably will continue to deteriorate over the next few years. With real per capita income lower than when he took office in 1980, Prime Minister Seaga fears—correctly, in our view—renewed social unrest should he comply with existing IMF stipulations to raise consumer prices on key imports or allow the Jamaican dollar to depreciate further. The IMF apparently will meet in January to consider a waiver to permit Jamaica to resume drawing on its $118 million standby program. Even if the Fund approves a waiver, Seaga's stated unwillingness to implement needed austerity measures would impede the country's ability to retain IMF funding in the coming months. Meanwhile, Jamaica's continuing economic decline will further erode Prime Minister Seaga's already weak popular support and boost the electoral chances of former Prime Minister Manley and his leftist People's National Party (PNP).

25X1

Seaga's Accumulating Problems

To rebuild the flagging economy he inherited from Manley, Seaga endorsed new policies designed to dismantle Manley's state-managed economic system and rejuvenate the private sector. Foreign funding by the IMF and Western donors in 1981 sparked the first real growth in Jamaica in eight years. This spurt, however, quickly fizzled in 1982 due to the deepening world recession and backsliding on Seaga's original promises to deregulate the economy. By yearend 1983, the island's ailing economy and Seaga's unwillingness to address the country's overvalued currency helped to derail the IMF program. After taking such steps as unifying the exchange rate and phasing out subsidies, Jamaica qualified in June 1984 for a one-year, $143 million standby agreement, but within six months noncompliance with IMF spending targets required a waiver to retain the Fund program. Economic output fell 1 percent in 1984. Inflation in this import-dependent economy reached 28 percent and unemployment hit about 30 percent—roughly the rate inherited from the Manley administration.

25X1

The Dismal 1985 Record

According to the World Bank, the Jamaican economy will contract 4 percent this year due to poor performances in key economic sectors. As a result, overall output in 1985 will barely match the depressed level in 1980:

- Virtually all domestic crops showed sizable declines during the first half of 1985. In addition, hurricane Kate in November reportedly destroyed several million dollars in crops, primarily fruits and vegetables destined for the US market.

25X1

- Kingston expects construction and manufacturing activities to drop more than 20 percent and 8 percent, respectively, compared with last year's already reduced level, largely because of high domestic interest rates, local credit restrictions, and shortages of raw materials, machinery, and spare parts.

- The tourist industry, buffeted by bad publicity from widespread demonstrations against oil price hikes last January and increasing crime, is expected to decline by $80-100 million; tourist arrivals fell 5 percent during the first eight months of this year, compared to the same period in 1984. In contrast, tourism in the Caribbean as a whole is up 6 percent this year.

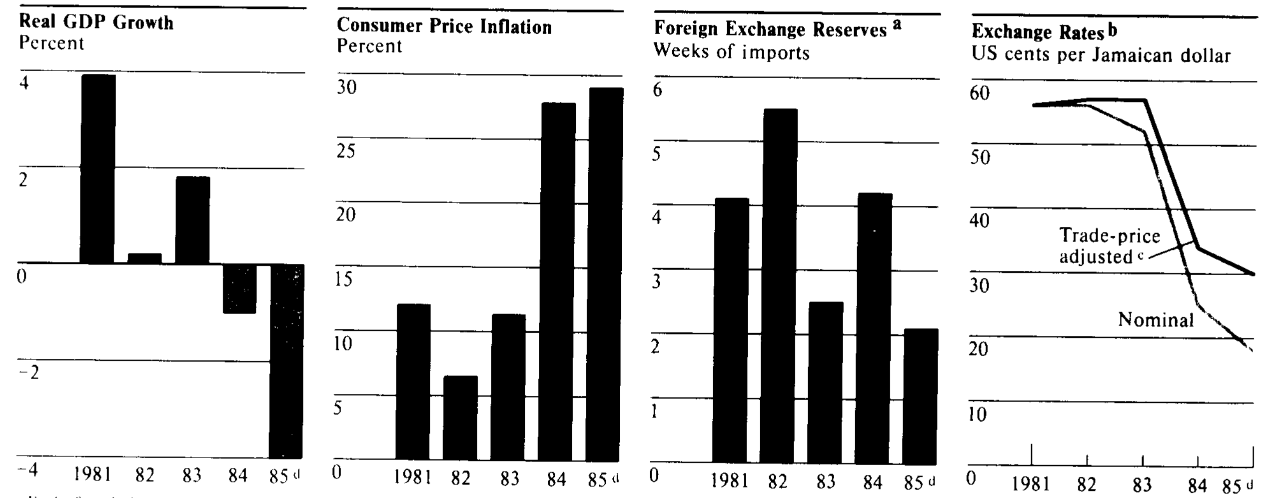
25X1

Perhaps most important, however, is the continuing decline in the production of bauxite/alumina—

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Jamaica: Economic Indicators, 1981-85



[a] End of period.
[b] Period average.
[c] Based on 1980 prices.
[d] Projected.

[redacted]

307669 12-85

25X1

after tourism, Jamaica's largest foreign exchange earner. Press reports indicate that bauxite and alumina output fell 42 percent and 14 percent, respectively, during the first six months of 1985. This slump resulted largely from the temporary closure of the ALCOA alumina refinery in February and weak world demand, which lowered production at other facilities. Moreover, the subsequent reopening of ALCOA in mid-1985 under a government lease arrangement was offset by the July shutdown of the ALPART refinery. According to government estimates, bauxite production in 1985 will be only 40 percent of the peak 1974 level. [redacted]

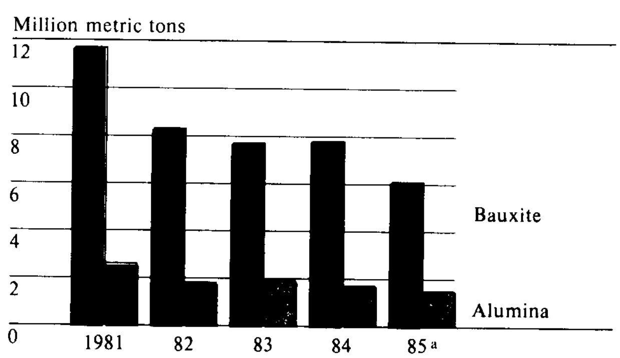
25X1

Developments on the foreign payments front are equally bleak. Based on Embassy [redacted] we believe the financial gap will total $50 million this year despite recent commercial bank and Paris Club debt reschedulings. During the first eight months of 1985 exports of bauxite, alumina, and sugar—which account for more than half of

25X1

25X1

Jamaica: Alumina and Bauxite Production, 1981-85



[a] Projected.

[redacted]

307668 12-85

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Jamaica: Balance of Payments, 1981-85

Million US $

	1981	1982	1983	1984	1985 [a]
Current account	−337	−400	−375	−306	−465
Trade account	−483	−619	−595	−438	−595
Exports (f.o.b.)	974	767	686	745	605
Bauxite/alumina	760	514	424	486	290
Other	214	254	262	259	315
Imports (c.i.f.)	1,457	1,386	1,281	1,183	1,200
Bauxite related	337	202	195	185	150
Other	1,120	1,184	1,086	998	1,050
Services (net)	22	69	118	5	−10
Travel	271	306	374	403	370
Interest payments/investment income	−201	−183	−185	−305	−270
Other	−47	−54	−71	−94	−110
Transfers (net)	124	150	102	127	140
Capital account	317	424	330	340	415
Public (net)	240	451	284	528	230
Private (net) [b]	1	20	−326	96	145
Short term (net)	76	−47	371	−284	40
Change in gross reserves	−20	24	−46	34	−50
External debt, yearend [c]	1,811	2,197	2,350	2,550	2,610

[a] Projected.
[b] Including errors and omissions.
[c] Guaranteed and nonguaranteed medium- and long-term obligations.

25X1

total exports—fell by 60, 28, and 30 percent, respectively, compared to the same period in 1984. We predict that the net foreign exchange loss in bauxite/alumina alone will be at least $150 million this year. Exports from other sectors—particularly light manufacturing and nontraditional agriculture—have increased sharply this year because of the depreciation of the Jamaican dollar, but still account for a relatively small share of the total.

Foot-dragging on limiting imports has compounded Jamaica's payments difficulties. In October, the Bank of Jamaica began supplying unusually large quantities of US dollars in local foreign exchange auctions to prop up the Jamaican dollar—which had slipped 30 percent since the end of 1984—and cap the rise in import prices. Moreover, Seaga, worried about a repetition of last January's widespread protests, refused to further reduce food and petroleum subsidies. As a result, local currency prices of foreign purchases have risen, but not sufficiently to reduce imports of food and gasoline—which together account for over half of total imports. 25X1 25X1

Jamaica's foreign payments problems worsened in September when the island failed to meet performance criteria—on net international reserves, domestic assets, and foreign debt arrears—under a

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

$118 million, 22-month standby agreement that had won IMF approval only two months previously. Seaga attributed the failure to the delayed arrival of $19 million in USAID funds. The IMF, however, believes that Jamaica would have missed the performance targets anyway. In an effort to salvage the standby program, Seaga has petitioned the IMF for a technical waiver. Moreover, in hopes of softening IMF terms, Seaga has requested that a joint IMF, USAID, and World Bank team visit Jamaica soon to analyze the economy with "fresh eyes."

Political Impact

Jamaica's mounting economic woes have reduced the already low standard of living for most Jamaicans. We expect real per capita GDP by the end of this year to fall to only 88 percent of the 1979 level, Manley's last full year in office. Despite the maintenance of subsidies, consumer prices rose 19 percent during the first eight months of this year. In addition, although Kingston claims the unemployment rate is 25.4 percent, we believe—based on Embassy and press reporting—that the actual rate remains closer to 30 percent; job losses in the bauxite and public sectors alone total at least 4,200 in 1985. This summer, following weeks of labor unrest, a three-day strike by public-sector workers protesting low government wage offers and increased layoffs nearly paralyzed the nation.

The country's deepening economic problems are spilling over into the political arena. A recent domestic public opinion survey indicates that Seaga's popularity has fallen to a record low and is little higher than that recorded by Manley in 1980. According to the survey, less than 25 percent of the polling sample support the ruling Jamaica Labor Party and most Jamaicans favor a change of government. Manley's political fortunes have risen accordingly; the poll indicated he and the PNP could win 61 percent of the vote—roughly Seaga's share in 1980—if a general election were held now.

Grim Near-Term Outlook

We believe that any recovery in the next few years hinges on Jamaica's ability to retain its IMF program, a prerequisite for stimulating investor interest, tapping foreign capital markets, and obtaining critical debt rescheduling agreements. Seaga, however, faces a serious dilemma because the Fund is likely to insist that the Jamaican dollar float freely and that the government phase out subsidies on food and petroleum. We believe these actions would lead quickly to significant price 25X1
increases and probably new social turmoil that would further erode Seaga's already slipping political support. 25X1

Even if Jamaica can retain the Fund program, any turnaround still depends heavily on economic diversification:

- In the unlikely event that world aluminum demand picks up significantly, US producers would continue to supply the bulk of their needs from lower cost operations, particularly in Australia, Brazil, and Guinea.
- The sugar industry—as in many Caribbean countries—will have to streamline production and processing to be viable in the long run.
- Rejuvenated growth in the tourist industry will turn on the strength of the US economy and 25X1 Kingston's ability to curb the recent upsurge in domestic crime, violence, and harassment of tourists by drug peddlers. Equipment shortages and growing morale problems in Jamaica's security forces stemming from recent budget cuts, as well as the increasingly entrenched drug network, work against much, if any, improvement on this front. 25X1

We believe that the best prospects for rapid gains are in nontraditional agriculture—particularly in high-value winter vegetables, spices, and cut flowers—and light manufacturing. The exports of both

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

sectors are eligible for preferential entry under the Caribbean Basin Initiative and other US trade arrangements. In addition, if the Jamaican dollar continues to weaken—as it probably would if allowed to float freely—these exports would become even more price competitive. [redacted] 25X1

These overall trends provide little hope that the Jamaican economy will stem its decline before 1987 at the earliest. Nor is Seaga likely to make any real headway in slashing unemployment or inflation. As a result, Kingston almost certainly will seek with an increasingly urgent tone, additional US aid, especially if—as we expect—the existing Fund program is scuttled. We believe Seaga will request help in such forms as additional bauxite purchases, support for the country's security forces, and highly concessional loans. We also judge that, despite steady US pressure, continued economic distress will further weaken Seaga's commitment to drug enforcement. Many Jamaican farmers will continue to view marijuana as a far more lucrative alternative to domestic crops. [redacted] 25X1

Seaga's term of office lasts until 1988, but if he is forced to call early elections—a distinct possibility—Manley would stand a reasonable chance of winning. We would expect a Manley government to depart from Seaga's economic policies in several key respects. Based partly on statements made at a recent PNP convention, we believe Manley's economic program would include a return to a fixed exchange rate and import licensing. The PNP also would not advocate divestitures of state-owned enterprises and cuts in government payrolls. Although PNP leaders have not ruled out pursuit of IMF support, enactment of these nonmarket policies probably would preclude a Fund program. The chances of Jamaica declaring a moratorium on its external debt—of which $700 million, or more than one-fourth, is owed to the United States—would increase. [redacted] 25X1

[redacted] 25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Areas Rich in Mineral Reserves

Boundary representation is not necessarily authoritative

25X1

706628 (545114) 12-85

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

China Nonferrous Metals Trade: From Imports to Exports?

25X1

China's drive for industrialization has created serious domestic metals shortages, especially in copper and aluminum, despite the country's vast untapped mineral resources. Beijing aims to double nonferrous metals production during its Seventh Five-Year Plan (1986-90), but inadequate infrastructure and a shortage of capital and technology are major stumblingblocks. As a result, China has had to substantially increase its imports of these metals in recent years. We thus expect the growth of metals imports to continue until new projects come on stream in the 1990s. As China's minerals industry develops, however, we believe that it could become an important new supplier of strategic minerals in the next decade.[1]

25X1

China: Metals at a Glance *Global Ranking*

	Reserves	Production	Exports
Aluminum	6th	8th	Not in top 10
Antimony	1st	1st	1st
Columbium	2nd	NA	NA
Copper	4th	Not in top 10	Not in top 10
Manganese	7th	5th	Not in top 10
Molybdenum	2nd	7th	In top 10 [a]
Nickel	2nd	10th	Not in top 10
Rare earths	1st	3rd	In top 10 [a]
Tantalum	1st	Not in top 10	Not in top 10
Tin	7th	7th	9th
Titanium	1st	5th	In top 10 [a]
Tungsten	1st	1st	1st
Vanadium	4th	3rd	3rd
Zinc	1st	Not in top 10	Not in top 10

[a] Rank unknown.

25X1

The Drive for Modernization and Supplies of Metals

China plans to quadruple its industrial output by the year 2000. This drive for industrialization requires large supplies of raw materials such as metals, but the country's current output remains far short of domestic demand.

25X1

China has a rich base of metal resources, but their development has been slow—due in part to a lack of necessary capital and technology—and in many cases has been confined to exploration by the provinces. The chief problem that will continue to limit mineral development is inadequate infrastructure. China's insufficient rail and road network prevents easy movement of equipment and supplies to remote regions, as well as transport of output to consumers or ports for export. In Xinjiang, for example, many minerals that are in short supply to the domestic economy have difficulty reaching the industrialized eastern regions. As a result, ports are congested, railways are overtaxed, and factories are forced to shut down at times because of shortages of delivered raw materials and energy. Moreover, until the infrastructure is improved, many mining projects will remain unattractive to foreign investors.

25X1

The Present Trade Picture

To meet industrial demand, imports of several metals—largely copper and aluminum—have reached alltime highs. While major production capacity expansion is under way, imports will continue to increase through the 1980s and much of the 1990s. After a marked decline in 1984, imports

[1] Two key strategic minerals—chromium and cobalt—are not found in large quantities.

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Secret Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Metal Production Plans

During its Seventh Five-Year Plan (1986-90), China aims to double nonferrous metal production, while consumption of nonferrous metals is expected to increase by 50 percent. The plan gives priority to aluminum, copper, lead, and zinc. To meet this goal, incentives are being instituted to attract foreign investment in this sector. China has already approached several Western countries—Japan, the United Kingdom, and the United States—on cooperative efforts such as countertrade, joint ventures, plant codesign, and projects financed solely by foreign investment. [redacted]

of copper, for example, have risen sharply in the first half of 1985. To help ease the copper shortage, Beijing is negotiating a deal with Codelco that will provide China with copper concentrate from Chile. [redacted]

Aluminum import needs are equally severe. Planners are under pressure to find guaranteed alumina sources overseas. [redacted] by yearend China may sign long-term contracts with several Australian alumina refineries for the purchase of approximately 150,000 metric tons of alumina in 1986, with the total expanded to 300,000 tons per year beginning in 1987. These contracts are expected to run for five to 10 years while China gears up domestic aluminum production. [redacted]

In contrast to the large imports of aluminum and copper, China is a major force in some metals export markets—particularly tungsten, tin, molybdenum, antimony, and rare earths:

- China's exports of tungsten, for example, account for one-third of total world tungsten trade and will continue to dominate this market.
- China's tin exports have been a factor in the inability of the International Tin Council to control the tin market.
- Smaller quantities of vanadium, manganese, and titanium are also exported. [redacted]

Outlook and Implications

We expect the general import and export trends of the last few years to continue into the 1990s. Although Beijing hopes that by 1990 some currently net imported metals such as aluminum, lead, and zinc will be available for export, we believe these hopes may be somewhat optimistic. On the other hand, China has the potential to become an even greater factor as a supplier of certain strategic metals. [redacted] 25X1

China's efforts to gain a greater share of certain strategic metals markets will likely cause increasing friction with other LDC and even Western competitors. China has come under increasing criticism in UNCTAD and other international forums, particularly the Primary Tungsten Association, for its high level of tungsten exports in the current depressed market. For example, at the International Tungsten Symposium in March, speakers from both producing and consuming countries identified Chinese exports as the major disruptive influence in the world market. The market for ammonium paratungstate (APT)—an upgraded tungsten product—is another area in which the United States and other producers claim increased exports have been disruptive. In the tin market, members of the International Tin Council, to which China does not belong, have accused Beijing of trying to undo the agreement through increased exports of tin. Finally, increased Chinese exports of tungsten and tin to Japan have angered traditional suppliers in the region, such as Australia, Malaysia, and Indonesia. [redacted]

25X1 25X1 25X1 25X1 25X1

More positively, China's need for advanced technology and equipment will open opportunities for suppliers such as Japan, the United States, Finland, West Germany, and the USSR. Development of its strategic minerals resources would make China an important additional supplier of these key materials. This would ease the risk of a supply cutoff for the United States, Japan, and Western Europe,

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

China: Apparent Trade in Nonferrous Metals, [a] **1979-84**

Million US $

	Exports						Imports					
	1979	1980	1981	1982	1983	1984 [b]	1979	1980	1981	1982	1983	1984 [b]
Total	**147**	**224**	**317**	**233**	**164**	**173**	**197**	**200**	**96**	**354**	**584**	**512**
Aluminum	29	78	131	103	62	60	119	123	73	210	139	97
Chromium	0	NEGL	1	NEGL	NEGL	0	0	0	0	0	0	0
Copper	5	9	16	20	17	18	29	47	6	67	306	162
Lead	NEGL	1	3	2	1	NEGL	23	17	13	6	3	1
Manganese	3	2	1	1	1	1	0	0	0	0	0	0
Nickel	0	0	NEGL	0	0	0	1	1	1	2	7	2
Platinum	0	1	2	3	4	2	10	1	1	1	NEGL	2
Silver	0	11	4	1	6	9	0	0	NEGL	NEGL	18	112
Tin	34	43	52	60	46	46	6	1	1	1	1	1
Tungsten	59	56	77	28	18	25	0	0	0	0	1	0
Zinc	5	7	12	8	3	1	NEGL	NEGL	1	68	103	130
Other [c]	12	16	17	6	6	11	8	9	0	0	8	6

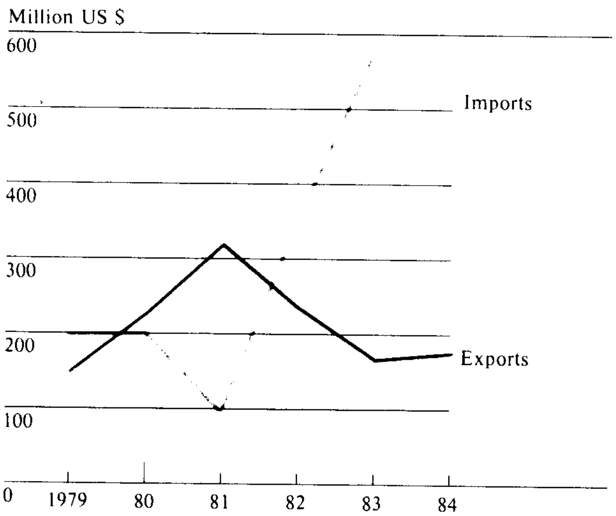
[a] Reporting countries: Australia, Austria, Belgium, Canada, Cyprus, Denmark, Finland, France, Greece, Hong Kong, Iceland, Indonesia, Ireland, Italy, Japan, Netherlands, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, Thailand, United States, United Kingdom, and West Germany.
[b] Australia, Hong Kong, Iceland, Spain, and Thailand have not reported for 1984.
[c] Includes beryllium, columbium, magnesium, molybdenum, tantalum, titanium, vanadium, and zirconium.

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

China: Metals Imports and Exports, 1974-84[a]



[a] Reporting countries include Australia, Austria, Belgium, Canada, Cyprus, Denmark, Finland, France, Greece, Hong Kong, Iceland, Indonesia, Ireland, Italy, Japan, Netherlands, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, Thailand, United States, United Kingdom, and West Germany.

307652 12-85

especially for platinum, titanium, columbium, and manganese, but could over the long run generate a dependency on China for some of these metals.

25X1

25X1

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Briefs

Energy

1985 OPEC Production Wrap-up

OPEC crude oil output is averaging 18.6 million b/d in December, a 1-million-b/d increase from November levels. Saudi Arabia captured most of the seasonal demand upswing, with output—based on current reporting—likely to average 5 million b/d in December. Total OPEC production for 1985 averaged 16.2 million b/d, slightly above the group's 16.0-million-b/d quota.

25X1

OPEC: Crude Oil Production, 1985 *Million b/d*

25X1

	1985 [a]	Quarter I-III	Quarter [a] IV	November	December [a]
Total	**16.2**	**15.7**	**17.9**	**17.6**	**18.6**
Algeria	0.7	0.7	0.8	0.8	0.8
Ecuador	0.3	0.3	0.3	0.3	0.3
Gabon	0.2	0.2	0.2	0.2	0.2
Indonesia	1.2	1.2	1.3	1.3	1.3
Iran	2.3	2.3	2.3	2.2	2.4
Iraq	1.4	1.3	1.7	1.7	1.7
Kuwait [b]	1.0	1.0	1.0	1.0	1.0
Less share of Neutral Zone	0.8	0.8	0.8	0.8	0.8
Libya	1.1	1.0	1.2	1.2	1.2
Nigeria	1.5	1.4	1.8	1.8	1.8
Qatar	0.3	0.3	0.3	0.3	0.3
Saudi Arabia [b]	3.5	3.2	4.4	4.3	5.0
Less share of Neutral Zone	3.3	3.0	4.3	4.1	4.9
UAE	1.1	1.1	1.2	1.2	1.2
Venezuela	1.5	1.5	1.5	1.5	1.6

[a] Estimated.
[b] Neutral Zone has no production quota; output is divided between Saudi Arabia and Kuwait and included in their country quotas.

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Spot Oil Price Developments

Prices for several key crudes have leveled off or rebounded slightly after plummeting early last week in reaction to OPEC's decision to defend a "fair share" of the world oil market. The prices of North Sea Brent and West Texas Intermediate, which fell by between $2 to $3 per barrel in two days of trading following the 8 December OPEC meeting, have rebounded $1 to $2 and now average $26 to $27 per barrel. Prices for these crudes are still as much as $4 per barrel below mid-November levels and close to their 1985 lows. Although 25X1 most analysts expect further price declines, the extent of market weakness will depend on how aggressively OPEC moves to increase market share. 25X1

Indonesia Pushes Oil Production to the Limit

Pertamina President Abdul Ramly has ordered foreign oil companies to boost crude oil production following OPEC's decision last week to recapture its share of the world oil market. According to US Embassy reporting, the directive could boost production from its current level of 1.25 million b/d to 1.5 million b/d, although limits on equipment and operating budgets could delay full production for up to 18 months. Indonesia's ability to sustain such a level over the longer term is uncertain. Although the country's crude oil and condensate production capacity will peak at about 1.6 million b/d by 1987, it will fall off 25X1 rapidly to 1.2 million b/d by 1990 as a result of reduced exploration in recent years, according to a UK-based energy consulting group. The reduction in exploration reflects inadequate incentives for foreign oil companies, which have long complained that they are overtaxed and that their production share, contractually set at 15 percent, has dropped to below 10 percent. 25X1

Colombia's New Oil Production

Commercial oil production from Colombia's Cano-Limon oilfield began earlier this month—at a rate of 30,000 b/d. The first segment of the 770-kilometer pipeline system has been completed and will carry the oil northwest to Rio Zulia, near the Venezuelan border. Existing pipelines will then transport the crude to the port of Covenas until a new pipeline network is completed. Initial capacity of the Cano-Limon to Covenas pipeline will be 100,000 b/d—if field conditions warrant, it can be expanded up to 200,000 to 250,000 b/d. Although terrorist activity continues to plague pipeline engineering and 25X1 construction firms, construction of the remaining portion is proceeding on time. Upon completion, total output will likely surpass 250,000 b/d boosting exports to about 100,000 b/d. Colombian crude exports will set back OPEC's attempts to encourage production restraint by non-OPEC producers. 25X1

Progress on French Nuclear Sale to China

France announced last Sunday an agreement in principle to construct a nuclear power station in Guangdong Province. China is to sign a letter of intent by 1 March. The 1,800-megawatt plant will use French reactors and British generators. The plant will be operated by a Chinese–Hong Kong joint venture and sell a share of the electricity to Hong Kong to help pay the costs. Equipment costs are estimated to be roughly $1.3 billion. Completion is scheduled sometime after 1991, but further delays are likely. The agreement followed the direct intervention of Vice-Premier Li Peng, China's energy czar. 25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Li is probably anxious to commit China to at least one imported nuclear plant during the 1986-90 Five-Year Plan in the face of pressure to reduce overall capital construction and "big ticket" items in favor of shorter-term energy projects to relieve already pressing shortages. [redacted] 25X1

International Finance

[redacted] 25X1

Nigerian President Rejects IMF

[redacted]

President Babangida's decision last week to stop negotiations with the IMF probably ends serious efforts at economic reform by his government. Babangida announced that the public debate he began after seizing power in August convinced him that Nigerians overwhelmingly favor a go-it-alone strategy. He also said that Nigeria will honor debt obligations to the best of its ability. Babangida probably has concluded that he does not have the political support for broad economic reforms. Despite the increase in oil production since September, the expected decline in world oil prices may slice export revenues by more than one-fourth next year. Lagos already cannot service its debts, and Babangida is likely to request a rescheduling of medium- and long-term commercial debt. [redacted] 25X1

25X1

Brooke Amendment Cutoff for Sudan Nears

[redacted]

Unless the Sudanese Government acts promptly, its inability or unwillingness to pay about $2.5 million in debt obligations will trigger a 31 December Brooke Amendment cutoff of all US assistance. Khartoum had, according to US Embassy reporting, hoped to postpone repayment pending a Paris Club rescheduling. No rescheduling agreement is likely, however, before the 31 December cutoff date, or even by 11 February when another $5.5 million in US debt becomes one year overdue. Khartoum may be testing US resolve to actually enforce a cutoff. Meanwhile, disagreement within the civilian Cabinet has thus far precluded approval of a much watered-down economic reform program that had received tentative acceptance from the IMF. [redacted] 25X1

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Morocco Misses London Club Payment

Morocco failed to make its first payment due under the London Club rescheduling agreement signed last October with Western banks. According to Ministry of Finance officials, Rabat missed the 6 December deadline because of inadequate foreign loans. Moroccan reserves currently 25X1 total under $50 million, less than half the September level. The rescheduling apparently allows Morocco 30 days' grace, however, before Rabat is technically in default. Senior officials claim that financial resources of state enterprises—such as the phosphate company—will be tapped if necessary to meet the 6 January deadline. In the meantime, Rabat is trying to convince a US bank to convert $10 million in debt now due into longer-term paper, which 25X1 would reduce the January payment to about $73 million. Largely because of problems in marketing phosphates, Morocco may well encounter similar payments problems in coming months. 25X1

Global and Regional Developments

EC-CEMA Dialogue Moves Slowly

The EC continues to withhold a response to CEMA's September proposal to open formal ties between the two organizations. The Community is concerned that the proposal does not sufficiently guarantee the status of potential bilateral commercial agreements between the EC and individual East European states. Previous talks broke down in 1981 partly because of CEMA's lack of a common commercial policy. In October the EC Commissioner for External Relations publicly suggested that EC-CEMA cooperation might be possible in some limited areas: the environment, economic forecasts, statistics, and industrial norms. Despite some advantages for East-West relations, EC-member states are wary of the Soviet Union exploiting a framework agreement 25X1 for political purposes. Recent US Embassy reporting indicates the EC may seek improved bilateral links with each CEMA-member state by early next year, with no reference to formal EC-CEMA ties. The EC has already agreed with Romania to expand their bilateral commercial agreement, the only one with a CEMA member. Negotiations for an agreement with Hungary stalled late in 1984, but Czechoslovakia reportedly wants to begin talks. 25X1

Dutch-Libyan Trade Agreement

The US Embassy in The Hague reports the Netherlands and Libya probably will sign trade and investment accords early next year—the latest in a series of Dutch initiatives to normalize relations with Arab states since the 1973 oil embargo. On the basis of data for the first nine months of this year, Libya's trade surplus with the Netherlands could be $400 million for 1985. The Dutch now export $160 million annually to Libya, and Dutch companies also receive a fee for processing Libya's oil. They may be interested in selling Dutch aircraft to Tripoli, and probably want to use the trade agreement to persuade Libyan leader Qadhafi to scale down his activities in Suriname. Qadhafi would 25X1 point to any agreement as another vindication of his regime's legitimacy and as proof of the ineffectiveness of US efforts to engineer a Western economic embargo against Libya. 25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Tunisian–Libyan Maritime Dispute Reviewed

In a unanimous decision the World Court has ruled against Tunisia for the second time in its dispute with Libya over rights to continental shelf areas thought to contain oil. The Court's decision lets stand the equidistant demarcation line determined in 1982. The line gives Tunisia 40 percent of the disputed territory, but precludes access to the most promising oil concessions. The decision also covers fishing rights in the Gulf of Gabes. Tunis has delayed plans to exploit the disputed territory since 1978, but probably was looking to offshore oil as an engine of growth in the next decade. While the Court's decision encourages bilateral negotiations to refine the boundary demarcation, tense relations with Qadhafi probably preclude any favorable adjustment in Tunisia's share. 25X1

25X1

Proposed Air Route Across Korean Peninsula

North Korea recently proposed to the International Civil Aviation Organization (ICAO) a Beijing-P'yongyang-Tokyo air route for which it claims air traffic controllers are already trained. A Korean peninsula route cutting 550 kilometers off the present Tokyo-Shanghai-Beijing route would probably interest Japanese, Chinese, Iranian, Pakistani, and US airlines. An ICAO proposal for both this route and a Beijing-Seoul-Tokyo route have been under discussion since early 1981 but has been repeatedly rejected by P'yongyang on the grounds that dual routes would perpetuate the division of Korea. We believe it highly unlikely that one route would open without the other or that North Korea would acquiesce to a service that could provide support to the 1988 Olympic games in Seoul. Moreover, both routes are close to the demilitarized zone where aircraft identification is a sensitive issue, and each provides opportunities for reconnaissance of industrial and military installations. 25X1

25X1

National Developments

Developed Countries

Japan Shelves Tax Reform for Another Year

The tax study councils of both the government and the ruling Liberal Democratic Party recommended this week that Tokyo delay a major overhaul of its tax system until FY 1987. Both councils opposed revising the present tax-exempt savings program or implementing a major personal income tax cut in FY 1986 which begins in April. The Finance Ministry is likely to heed these recommendations in its current budget compilations, even though Prime Minister Nakasone favors sweeping tax changes to help ease trade frictions by expanding domestic demand. Tokyo's commitment to budget austerity, strengthened by the projected tax revenue shortfall resulting from the impact of the stronger yen on corporate profits, leaves the government little room to maneuver on tax reform in FY 1986. Tokyo is instead likely to adopt a small income tax cut and minor tax incentives for housing, offset by a larger rise in corporate taxes. The prospects for substantial tax reform in 1987—including the adoption of a national indirect tax to offset revenue losses from a personal income tax cut, will depend in large part on the support of Nakasone's successor—his term expires next fall. 25X1

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

[redacted] 25X1

Tokyo Continues Opening Telecommunications Market

In an apparent reversal of its hard-line stance, Tokyo has decided to allot frequencies for portable data terminal services, according to the US Embassy. Restrictions on radio wave equipment imports are the last stumbling block in this round of bilateral telecommunications market-opening negotiations, and their removal allows US manufacturers to sell portable data terminals in Japan with only minor technical modifications. Industry sources told the Embassy US sales in Japan would probably total only about $2 million in 1986, but the total market is expected to reach $100 million in five years and could easily expand to $150 million. Quick liberalization of the market is essential. Although US firms will be unchallenged in the short term, a competitive Japanese product will probably be introduced in 1987 or 1988. We believe this is part of a serious attempt by Tokyo to reach a successful conclusion to telecommunications negotiations, and suggests other bilateral trade talks will probably not be seriously affected by recent US actions involving Japanese semiconductors and leather restrictions. [redacted]

[redacted] 25X1

25X1

25X1

[redacted]

25X1

25X1

[redacted] [redacted]

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

[redacted] 25X1

French Economic Policy Dispute

The conservative opposition, which seems likely to win control of the government in elections next March, is bracing for a struggle with President Mitterrand over control of France's international economic policy. [redacted] The conservatives expect the new prime minister to insist on accompanying Mitterrand and to try to dictate the French position, especially on the issue of preparations for the new GATT round. [redacted] Infighting may lead to a temporary paralysis of policy while Paris sorts out how to share power between a Socialist president and a conservative government. Mitterrand, in an effort to avoid embarrassing domestic squabbles, probably will keep a low profile at Tokyo. If pressed hard by the Cabinet, however, he may play the spoiler, especially on trade issues, where the conservatives favor a tough line for France. [redacted]

25X1 25X1 25X1 25X1 25X1 25X1 25X1

Progress on West German Financial Liberalization

The Bundesbank will soon allow banks to issue certificates of deposit and similar short-term instruments, according to the US Embassy. These new instruments should be especially attractive to foreign investors and will complement last May's liberalization of the foreign bond market. The Bundesbank has historically discouraged foreign investment in domestic capital markets, fearing that intensified capital flows would weaken monetary policy. The Bundesbank may still be cautious about an increase in the mark's limited role as a reserve currency, but feels that West Germany must keep pace with liberalization elsewhere or be eclipsed as a financial center. The nation's largest bank, for instance, recently transferred its capital operations from Frankfurt to London because of that city's more liberal trading environment. West Germany's new capital markets will require time to develop, and we do not anticipate that increased liberalization will significantly affect the volatility of the mark. [redacted]

25X1 25X1

Worsening West German Labor Relations

West Germany's labor unions have vowed to strike if pending legislation restricting unemployment benefits is approved. The bill would deny unemployment benefits to nonstriking workers who are laid off or locked out because of strike activity, but who stand to benefit if the strike succeeds. Last year, for example, some unions launched "focus" strikes by small numbers of key personnel in an attempt to force a 35-hour workweek, while conserving strike funds. The Free Democrats, Kohl's coalition partners, and conservative

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

members of Kohl's own party have pressured the Chancellor to end what they contend is government subsidization of strike activity. If government and labor are unable to avoid a confrontation over the issue, West Germany's once enviable record of labor relations will be sullied further. The dispute could even sour next year's negotiating round, which will focus on wage demands. 25X1

Belgian Government To Continue Austerity Program

The economic program of the newly formed Martens VI coalition of Social Christians and Liberals will continue the four-year austerity program begun under the previous coalition. The government intends to reduce the budget deficit from about 11 percent of GNP this year to 8 percent by 1987 and 7 percent by 1989. Because the partners have rejected tax increases or new taxes, Brussels is likely to attack the deficit with cuts in business subsidies, unemployment compensation, and civil service personnel costs. Many of the 25X1 cuts are in politically sensitive programs, and the government will find it difficult to trim the approximately $770 million needed to meet its 1986 goal. Moreover, a shortfall in revenues is expected because of slower than projected growth and preelection pledges of a 2.5-percent cut in personal income taxes over the next three years. 25X1

Spanish Unemployment Increases

Registered unemployment rose in October for the second straight month following five consecutive months of decline. The October rate of 20.1 percent is up 0.8 percentage point since August and is only 0.1 percentage point below the record set in March. Most of the recent increase is due to a rise in the number of young people entering the job market and a decline in activity in the tourist and agricultural sectors. Although the number of unemployed grew by only 64,000 in the first 10 months of 1985—in contrast to an increase of 235,000 a year earlier—structural problems continue to prevent any substantial improvement in the unemployment rate. More jobs are likely to be lost as 25X1 the Gonzalez government pursues industrial restructuring and when Spain joins the EC next month and is forced to open its markets to its West European partners. 25X1

Portugal Eases Economic Policy

Prime Minister Cavaco Silva's new center-right government has announced a series of measures aimed at promoting economic development and reducing state control over the economy. The new program—which effectively reverses the austerity policies of former Socialist Prime Minister Soares—includes a four-point cut in domestic interest rates, a revision of rigid labor laws and a series of tax cuts for 1986. The stimulatory measures, however, are likely to be short lived because the resulting increase in domestic demand, coupled with the liberalization of import barriers required when Portugal enters the EC next month, could lead to a 1986 current account deficit as large as $1 billion. This 25X1 may force Lisbon to seek EC or IMF financial support—support that almost certainly would be contingent on a return to more restrictive economic policies. 25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Less Developed Countries

Nicaragua Controlling Exchange House Operations

Increasing government control over Managua's private currency exchange operation—set up last spring by the Sandinistas to undercut black-market activities—has greatly reduced currency transactions through legal channels. The exchange's rates—fixed by the government—are less than three-fourths the street value. As a result, the exchange has had to limit dollar sales by requiring customers to apply a week in advance and present a visa and airline ticket to obtain up to $500, according to US Embassy reports. The exchange operation is also trying to establish a relationship with an international financial institution to facilitate transfers of dollars from the United States to Nicaraguan residents. While the new currency transfers would relieve financial pressures on some individuals, they are unlikely to be enough to strengthen the cordoba. Managua probably will have to remove exchange rate restrictions if its currency operation is to stay in business. 25X1

25X1

El Salvador's Economic Policy Initiatives

The stabilization package President Duarte is preparing could end 18 months of economic policy drift but is unlikely by itself to restore business confidence in the near term. The program—scheduled to be announced early next month—includes major initiatives to increase taxes and limit domestic credit. It also effectively devalues the colon by about 20 percent. To offset the social costs, Duarte is promising new fuel subsidies and a wage hike. Few sweeteners, however, have been offered to the private sector, which Duarte continues to denounce for its lavish consumption. While this program gives no direct production incentives, Salvadoran policymakers note that an export promotion law is likely to be passed soon by the Assembly and a new foreign investment code is under study. In addition to business opposition, Embassy reports indicate that some of the leftist-dominated labor unions already are planning strikes to protest the increased austerity. 25X1 25X1

Trinidad and Tobago Discouraging Labor-Intensive Investment

Recently enacted legislation supported by influential labor groups will further discourage investment in labor-intensive industries at a time when Trinidad and Tobago's unemployment rate—now 25 percent—is rising. The new law requires employers to make lump-sum payments—based on length of service—to laid-off workers and gives such payments a priority claim on the assets of a liquidated firm. Such preference will discourage banks from making business loans. Moreover, fearing a sizable financial burden from future layoffs, existing firms will hesitate to expand payrolls, while new investors—foreign and domestic—will be reluctant to commit funds to operations requiring substantial labor input. Labor-intensive investment in Trinidad has long been deterred by high labor costs, which have been amplified by the government's previous unwillingness to devalue the Trinidadian dollar. 25X1

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Suriname Seeking Economic Support

Suriname's worsening economic plight is prompting the Bouterse regime to court virtually any country offering hope of financial support or expanded trade:

- Despite Libya's failure to deliver a promised economic package reportedly worth as much as $100 million, Suriname appears to be expanding ties to Tripoli; a Libyan delegation recently visited Suriname to discuss increased economic cooperation.
- Taiwan has provided a $40 million credit line.
- Brazil has opened a $20 million credit line and agreed to purchase more Surinamese alumina. 25X1
- Colombia has agreed to a $10 million credit line.
- China has made a $7 million, interest-free loan to finance construction of an indoor stadium.
- Venezuela has provided a $3 million credit line and agreed to help develop Suriname's fishing industry.
- Czechoslovakia apparently has agreed to supply capital goods in return for bauxite and related derivatives.
- Iranian representatives reportedly have visited Suriname to explore expanding trade relations. 25X1

Largely in hopes of attracting Western assistance—particularly a resumption of $600 million in Dutch aid suspended in 1982—Head of Government Bouterse last month gave leaders of three previously banned political parties a limited voice in his policymaking council and pledged to return Suriname to democracy by April 1987. Nevertheless, Bouterse's recent steps toward democracy are unlikely to prompt the Netherlands to release its blocked aid. Unless Suriname's economic situation improves dramatically—an unlikely prospect—the regime probably will continue to make at least token steps toward democratization to attract Western donors and boost its low domestic popularity 25X1

Donor Response to Mauritanian Reforms

During the inaugural donors' meeting for Mauritania in Paris last month, Nouakchott's Western creditors applauded the government's recent austerity measures. The donors pledged about $60 million to underwrite additional adjustments during 1986-88 promising more funds as needed. The IMF also indicated Mauritania's solid performance would permit negotiations to begin soon for a second 12-month standby. Nouakchott still faces severe economic difficulties, however, as continued weak prices for iron ore preclude any improvement in an already unacceptably high unemployment level and double-digit inflation. Neither is there any prospect for a turnaround in the country's chronic food shortage. Moreover, harsher austerity will complicate the government's efforts to establish a sufficient degree of stability to justify a return to civilian rule. The Taya government will have to carefully allocate aid monies to avoid charges leveled against previous regimes of rampant corruption and favoritism of Arabs over Black Africans. 25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Botswanan Drought Persists

Botswana's agricultural prospects appear dismal as the country enters its fifth consecutive year of drought. Seasonal rainfall in most areas is 50 to 75 percent below normal. The cattle industry, the country's second-largest source of foreign earnings, will very likely suffer additional losses due to worsening grazing conditions. Total crop production, normally 25 percent of national requirements, is expected to drop to 10 percent. In addition to boosting commercial imports, Gaborone will likely seek food aid from the United States and other foreign donors to make up the deficit. 25X1

25X1

Gloomy Budget for Sri Lanka

Sri Lanka's budget for 1986 underscores growing strains in the economy. Debt service will take one quarter of total outlays and is continuing to grow. Defense spending officially is scheduled to decline slightly, but only because supplemental appropriations in 1985 increased defense expenditures by some 80 percent from the original projection. Nonetheless, defense spending will eat up about 9 percent of the budget, compared to 3 percent in 1982. The government shows no willingness to cut welfare spending or subsidies for public enterprises; development projects, already hit, are likely to face additional cuts. Colombo is not proposing any significant structural revisions in the tax system but is 25X1 relying on increases in excise taxes and other fees to bring in additional revenue. Nevertheless, the budget deficit is likely to exceed 40 percent of total spending. The tax increase, plus the high level of government borrowing necessary to cover the deficit, will add significantly to inflationary pressures.

25X1

Indonesian Bankers Press for Spending Increases

The Chairman of the Private National Banks Association of Indonesia last week publicly urged the government to rapidly disburse unspent development funds, claiming that monetary expansion alone is insufficient to reverse the economic slump. We estimate real economic growth this year of only 3.1 to 3.5 percent. According to US Embassy reporting, the bankers believe that easier monetary policy and increased commercial bank credit will do little because businesses—particularly the textile and electronics industries—are seriously handicapped by weak demand. They also argue that Indonesia's relatively low savings rate and the lack of an efficient long-term capital market is a major disincentive to private investment. In our view, however, it is unlikely that President Soeharto will retreat soon from austerity measures already in place. 25X1 Increased government spending in the face of declining petroleum revenues would undoubtedly aggravate federal budget and current account deficits—thereby rapidly expanding the country's yearend 1985 foreign debt of $37 billion. 25X1

Communist

USSR Renews Grain Agreements

Moscow has agreed to renew two five-year grain agreements with Canada and Argentina. The Soviets, at a minimum, will buy 25 million metric tons of Canadian grain over the period of August 1986 to July 1991 and 4 million tons of Argentine corn and sorghum annually. The Argentine pact reportedly also

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

includes 500,000 tons of soybeans. These agreements, along with the existing long-term agreement with the United States, commit the Soviets for the next several years to annual grain imports averaging 17 million tons—at a cost of about $2 billion per year at 1985 prices. The renewal of the long-term agreements suggests that Moscow considers the USSR's grain production goal—a 70-million-ton increase over the 1981-85 average by 1990—risky at best. [redacted] 25X1

Soviet Trade Ministry May Be Reorganized

[redacted]

A Soviet official has told the US Embassy that a reorganization of the Ministry of Foreign Trade is likely early next year. The proposal now in favor would reduce the number of foreign trade organizations responsible for negotiating contracts from 47 to about 10 by forming trading groups for each broad commodity group. The plan would also bring the trade organizations that are outside of the Ministry under its jurisdiction and reduce by half the number of deputy ministers. General Secretary Gorbachev probably hopes to import machinery and equipment more efficiently. The proposed plan would also remove those officials who are likely to block further changes in the foreign trade system. It does not appear to address the key problem of unresponsiveness by foreign trade organizations to the needs of end users. 25X1
[redacted] 25X1

25X1

[redacted]

Highway Construction in China's New Five-Year Plan

[redacted]

China's stated emphasis on highway construction for the Seventh Five-Year Plan (1986-90) will not eliminate transport bottlenecks in the 940,000-kilometer road network. Because of increases in domestic production, foreign trade, and vehicle availability, traffic volume is growing faster than road capacity. About 60,000 kilometers of roads were built in the past five years and the new five-year plan will add only another 70,000 kilometers. Little of the new construction will be directed toward developing a national highway system. Beijing needs to concentrate on developing limited access highways for long-distance truck traffic between ports and interior points—only 200 kilometers of such highway was built during the last five-year plan. Currently, port access roads are clogged with slow-moving traffic including everything from wheelbarrows, animal drawn carts, and bicycles to modern cars, buses, and trucks. [redacted] 25X1

25X1

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

25X1

Page Denied

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7

Sanitized Copy Approved for Release 2011/03/07 : CIA-RDP97-00771R000807820001-7