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EGYPT-CYPRUS

Palestinian extremists opposed to Egyptian President Sadat's Middle East peace initiative struck at his regime by assassinating leading Egyptian editor Yusuf Sibai in Cyprus late last week. The killing has provoked a groundswell of anger in Egypt against Palestinians. It also led to a break in relations between Egypt and Cyprus after Cypriot troops frustrated an attempt by Egyptian commandos to capture the terrorists at Larnaca Airport in Cyprus and free hostages they had taken. Fifteen commandos were killed in the abortive operation.

Egypt is apportioning blame for the events equally among Arab opponents of

Sadat's peace initiative and Cypriot officials—although Egyptian ineptness appears to have been a major factor in the fiasco at Larnaca. The ill-fated commando operation has probably damaged Sadat's prestige, but his domestic position remains strong.

Anger Toward Palestinians

The assassination of Sibai has led to public condemnations in Egypt of Palestinians of all stripes. The killing is unlikely, however, to impact significantly on Sadat's efforts to provide for Palestinian self-determination in any settlement with Israel. Sadat must consider a number of political imperatives, such as the need to include other Arabs in peace negotiations, and is unlikely to reverse his policies because of a single terrorist attack by opponents of those policies.

Egyptian leaders have tentatively concluded that the Black June terrorist

organization ordered Sibai killed. Black June is aligned with the extremist Palestinian "rejection front" and operates from Baghdad with Iraqi support. It was originally formed to protest Syrian intervention in Lebanon in 1976, but in recent months it has apparently begun a campaign against Arab officials who support a peaceful resolution of the Arab-Israeli conflict. The organization is led by Sabri al-Banna—alias Abu Nidal—who was sentenced to death some time ago by Yasir Arafat's Fatah group for conducting unauthorized terrorist operations.

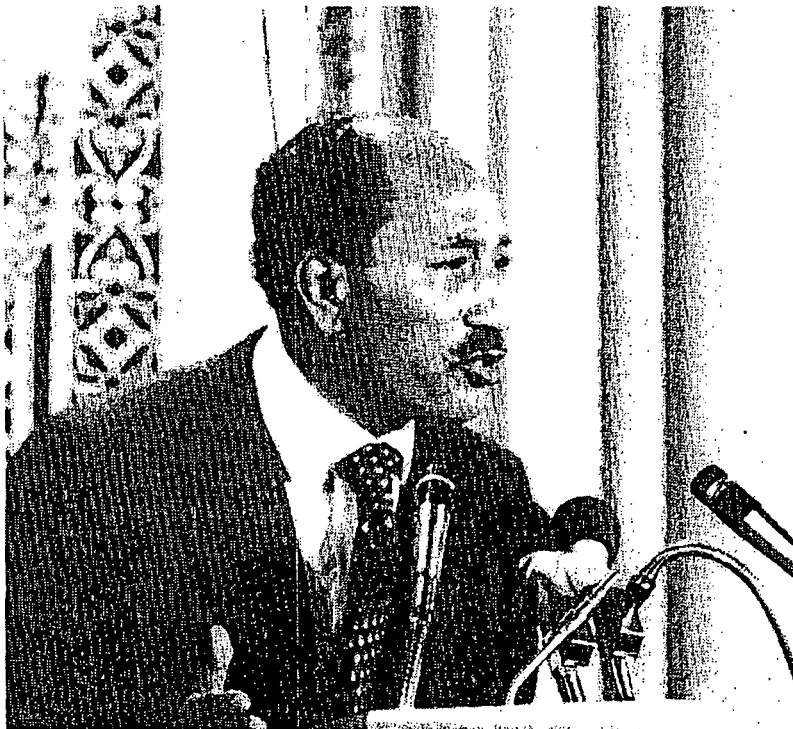
Egyptian leaders have not yet reacted openly to apparently accurate reports that a special unit of the Palestine Liberation Organization—which is headed by Arafat—was sent to Cyprus to assist the Cypriot National Guard and that it participated in the fighting. Arafat wants to keep open his lines to Egypt and is unlikely to have authorized the unit to join in the fighting against the Egyptians. It may have inadvertently been involved, however, because of its proximity to the action.

Condemnation of Cypriot Role

Egyptians from Sadat down have bitterly condemned the Cypriot role in blocking the commando raid. They have accused Cypriot President Kyprianou of treachery and raised the question of Cypriot collusion with the terrorists. Sadat argues that Cypriot leaders shirked their responsibility to oppose international terrorism.

Sadat and other Egyptian officials have hinted strongly that Egypt will alter its traditional support for Greek Cypriots against Turkey if the two Palestinian terrorists are not extradited to Egypt or swiftly punished by the Cypriots. In the past, the Cypriots have been lenient in their treatment of terrorists.

The Egyptian public for the most part has reacted to the events in Cyprus by rallying to Sadat and the military. More educated groups, however, are said to recognize ineptness in Egypt's handling of the situation, and there are reports that those responsible for planning the raid are trying to mask their bungling.



Despite the Cyprus raid, President Sadat's domestic position remains strong

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EGYPT

Egypt's financial outlook has improved substantially during the last few months. Because of soaring private transfers and favorable oil production prospects the country's unfinanced payments gap—which had been expected to be about \$1 billion annually through 1979—is likely to be halved over the next two years.

Unexpectedly large worker remittances from abroad last year left Egypt with a \$500 million surplus to apply to 1978 bills. This year, voluntary private transfers are expected to total \$1 billion—twice the amount projected six months ago.

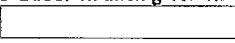
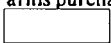
Most of the increase is coming in through the black market that the government tolerates despite opposition from banking circles. Egyptian financial authorities realize a crackdown on black market operations would have to be accompanied by a devaluation of the exchange rate used by the banks for handling private remittances, in order to avoid drying up the source of payments.

An ambitious \$500 million development bond drive currently under way is also boosting transfer payments. Banks in Egypt were the main subscribers to a similar \$200 million bond drive last year. The new drive, however, involves a stronger promotional effort outside the country, especially among expatriate Egyptians in Saudi Arabia; they are expected to be important subscribers.

Before the end of 1979, oil exports from newly discovered fields may narrow the payments gap still further. A West German-led consortium will shortly begin development of a large new oilfield in the Gulf of Suez. Egypt's share of the field's initial output should be \$300 million annually and the long-term earnings prospects are excellent.

At the same time, the states of the Gulf Organization for the Development of Egypt—Saudi Arabia, Kuwait, Abu Dhabi, and Qatar—have softened their attitude toward providing Cairo with substantial import financing. The organization agreed late last year to make \$550 million in cash payments to Egypt to finance imports—an abrupt about-face from the organization's earlier intention to reserve remaining assets for project aid.

In January, officials of the Saudi-sponsored organization indicated that as much as \$1 billion in cash aid might be available to Egypt this year for imports. The four Gulf states will provide about the same amount for project aid.

Cairo's need for such Arab cash subsidies in 1978 and 1979 seems likely to be greatly reduced, however, and could be eliminated entirely if private remittances remain high, the new oilfield in the Gulf of Suez comes into production quickly, and an Egyptian request for \$800 million in additional US aid is approved. Egypt will continue to need Saudi financing for its arms purchases. 


ISRAEL

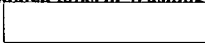
Divisions within the Israeli cabinet over the issue—critical to Middle East peace negotiations—of future Jewish settlements in occupied areas were brought into sharper focus early this week when the first of two special cabinet debates on the question was held in Jerusalem. The second debate, to be held on 26 February, may produce a stopgap solution, but Prime Minister Begin is likely to continue to be bedeviled by cabinet dissension over this issue.

Defense Minister Weizman has emerged as the chief spokesman for a more flexible approach on the settlement question with Agriculture Minister Sharon, the leader of a group of hardliners. Weizman, the leaders of the Democratic Movement for Change, and the Liberal faction of Begin's Likud grouping clearly favor a freeze on settle-

ment activity pending the outcome of negotiations with Egypt. In pressing for a moratorium, they hope to improve the atmosphere for talks with the Egyptians and undo some of the damage that has been done to Israel's image abroad, especially in the US.

Sharon and other "hawks," including spokesmen for another Likud faction, on the other hand, want to accelerate the settlement process in the Sinai and on the West Bank as a hedge against any softening in the government's negotiating position.

Begin, whose views will be decisive, thus faces sharply divergent pressures. If he orders a standstill, Sharon could threaten to bolt the cabinet, driving a wedge among Begin's supporters on the right. But if Begin supports a resumption of settlement activity, it will complicate his relations with moderates within the ruling coalition. Weizman and the Liberals, while unhappy, would not oppose Begin openly, but leaders of the Democratic Movement for Change would be under strong pressure from "doves" in their party to challenge the government and even drop out of the coalition.

Thus far, the Prime Minister has reserved his position, although there have been Israeli press reports that he may be leaning toward supporting a temporary freeze on new settlement activity for tactical reasons. To avoid the appearance of giving in to outside pressure and to mollify Sharon, however, Begin may decide on a middle course, perhaps by simply extending the present suspension on settlement activity in the Sinai at least until after his scheduled talks in Washington in mid-March. 

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