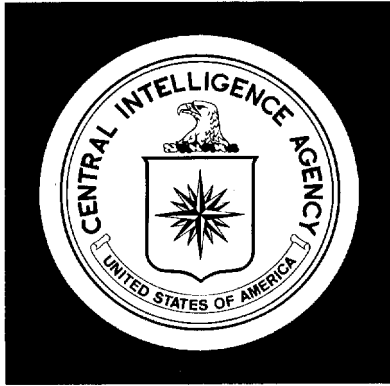


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# Weekly Summary

## Special Report

*Peru: The Revolution Moves On*

State Dept. review  
completed

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# PERU

## The Revolution Moves On

*"It is absolutely indispensable to re-orient and re-build all of the state apparatus. A new socio-economic order, a new system of ownership, in a word, a new society, calls for a new type of government structure. The revolution of the armed forces will carry out a process of change in the economic, social, political, and cultural structures in order to attain a new society in which the Peruvian man and woman can live in freedom and justice. The armed forces, as promoters and principal supporters of the Peruvian revolution, will conduct the process of change until it has become irreversible." (emphasis added).*

President Juan Velasco Alvarado, July 28, 1974.

Special Report

September 3, 1974

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### Summary

When the Peruvian armed forces, led by army General Velasco, took power from the duly elected president, Fernando Belaunde Terry, on October 3, 1968, most observers branded it simply another "palace coup" by pro-Western reactionaries. Within days, however, it became apparent that what was happening was more than a traditional military *golpe* perpetrated by disgruntled, status quo - oriented generals. Starting with the take-over of the large, US-owned International Petroleum Company refineries on October 9, 1968, and continuing through a series of agrarian, labor, and peasant reforms, the Velasco government has engaged in a wide-ranging process designed to re-orient Peruvian society completely away from the oligarchs and "foreign influences." Now, six years later, this process continues at an even faster rate, despite the fact that the military is still viewed with suspicion—if not hostility—by most Peruvians.

President Velasco has consistently and proudly maintained that the Peruvian revolution is "neither capitalist nor communist." Clearly, however, the emphasis has been on expanding state control of the economy and denying virtually any popular participation in the decision-making process. The timetable for instituting reforms remains purposely vague, but government leaders mince no words in telling the country that the "participatory democracy" so loudly touted by Velasco is still far from fruition.

### Velasco and His Successor

The military-led revolution that began in 1968 strongly reflects President Velasco's views. He has been the most dynamic force behind the extensive program of domestic reform and foreign policy independence. Even though Velasco may be nearing the end of his tenure as chief executive, the revolution has been sufficiently institutionalized that the process will continue to mirror his attitudes after he leaves office.

Velasco is fully aware of the key role he has played in shaping the military-led revolution, but he knows he must step down eventually. He survived a near-fatal ruptured abdominal aneurysm in 1973 that cost him one of his legs. Although Velasco is active and dynamic at present, continuing medical problems could lead to a worsening of his condition at any time.

It is a foregone conclusion that his successor will be another army general—either a "radical"

(i.e., one favoring a strongly nationalistic foreign policy and an accelerated program of domestic radicalization) or a "moderate" (i.e., one more amenable to compromising with the US in foreign policy and favoring a slower and more deliberate approach to domestic reforms). Whoever succeeds Velasco, however, is not likely to alter the basic thrust of Peru's nationalistic and socialistic revolutionary experiment.

Although it will be the revolutionary junta—consisting of the chiefs of the three services—and not Velasco who will choose a new president, Velasco's views will weigh heavily in any deliberations. His present inclination is to name General Jose Graham Hurtado, who heads the influential Presidential Advisory Committee. Graham shares the President's radical views, but Velasco may still harbor reservations about his ability to carry out further revolutionary reforms. This concern for deepening the revolution has in turn prompted Velasco to name the army chief of staff, Francisco Morales Bermudez Cerrutti, to

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Morales Bermudez

Graham

become prime minister and minister of war next January.

Morales Bermudez, who served as minister of economy and finance from 1969 to 1973, is a leading moderate and has received credit for keeping Peru's economy afloat during these years. By keeping Morales Bermudez in a high government post, Velasco apparently hopes to take advantage of his proven pragmatism and his ability to get the job done, despite basic ideological differences between the two men. Although the prime ministership would seem to be the stepping stone to the presidency, Velasco now appears less willing to allow a moderate to succeed him than previously.

The extent of General Graham's support among key military leaders is not clear, but he is a loyal *velasquista* and probably could count on the support of most, if not all, of the army troop commanders. Important troop commands are in the hands of officers personally loyal to Velasco.

More moderate military leaders, including Morales Bermudez and Interior Minister Pedro Richter Prada, are in a weaker position now than a year ago. Under present circumstances, the moderates probably would be neither able nor willing to risk a decisive confrontation with the radicals to dispute the accession of Graham to the presidency. The navy—traditionally the most conservative service—is inferior to the army in both military and political power, and its current

minister, Admiral Jose Arce Larco, has sold out to Velasco in spite of traditionally strong animosities between the two services. General Rolando Gilardi Rodriguez, chief of the air force, also is in general agreement with Velasco's policies; he would probably support the President's choice of a successor unless it appeared that this would severely damage armed forces unity and effectiveness. One objection that might be raised by Peruvian officers—who are great respecters of seniority when it comes to filling high government posts—is that Graham is junior to Morales Bermudez. At this point, however, Velasco appears intent on radicalizing the revolution and thus would rather support Graham than Morales Bermudez. In the unlikely event that Velasco were forced from office, the scenario would become more complicated, with additional generals probably contending for the presidency.

#### Domestic Issues

Lack of popular support, especially in the past year, seems to have prompted Velasco to become even more high-handed and to accelerate the revolutionary process. This in turn has brought increasingly authoritarian measures, such as the forced resignation of a group of high-level naval officers and the expropriation of the country's major daily newspaper in July. These recent authoritarian moves reflect the President's personal sensitivity to criticism from any quarter; there is also a sincere belief among top military leaders that they as a group know what is best for Peru and are uniquely qualified to carry out the essential changes.

Both of these events have brought major issues to the fore. The ousting of Vice Admiral Vargas as navy minister last May made public the most serious inter-service split since the military took power. The press take-over sparked three days of anti-government demonstrations, which for the first time were led by middle-class activists in Lima. As the middle class becomes more actively involved in opposition activities, possibly including terrorism, support for Velasco by moderate military leaders could begin to erode. By using such tactics, businessmen and civilian political groups may try to convince military

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leaders that a continuation of Velasco's radical policies would bring chaos to the country. If such demonstrations recur, and if the opposition becomes more violent, moderate military leaders may come to believe the pace of socialization must be slowed if any semblance of national unity is to be maintained.

Although President Velasco frequently asserts that his government is establishing a "participatory democracy," he apparently does not intend to allow the "people" to assist the armed forces in setting national policies for the foreseeable future. The government has made some effort, however, to allow the working class and peasantry to participate in implementing these reforms through organizations such as social property enterprises and the ubiquitous National System of Support for Social Mobilization (SINAMOS), an organization designed to create popular support for the revolution. In addition, the government maintains contact with the Peruvian Communist Party.

The dialog between the military and the Communist Party does not reflect any government affinity with the party or its ideology, although some government officials do sympathize with its goals. Velasco and most of his associates, however, view the party as a channel of communication with the lower class and as a consistent supporter of government programs. Also, the President has tried to use the party to help suppress anti-government demonstrations, with little success. The dialog is likely to continue.

Contacts between the military and the mass-based opposition American Popular Revolutionary Alliance (APRA) wax and wane, and are clouded by 40 years of animosity. Still, there are those within the government who see in APRA, with its tradition of advocating non-Marxist economic reforms, a means of gaining more permanent and widespread support for the government's programs. Others, including Velasco, remain deeply suspicious of any civilian political organization and may lean toward eventually forming a separate, government-controlled party.

There are a large number of civilian experts serving in the military government, but only a handful really participate in the high-level decision-making process. This reflects the military's disdain for civilians as well as the general lack of rapport between these two groups. If, as is likely, middle-class opposition to the government increases, this group's access to top military leaders will be even more restricted. Civilians of more radical persuasions, on the other hand, may gain entree to the government. Those few civilians who have access to Velasco's inner circle have a long association with the President personally, and appear to share his views on domestic and foreign policy. Personal ambition may play a more important role than ideology in determining what line these civilians are willing to support.

The military's low regard for civilian politicians has been repeatedly demonstrated. In May, the government outlawed the Popular Action Party of former president Belaunde, and early in August, following the anti-government disturbances, arrested several of its officials.

The one party that the regime has not moved against decisively, however, is APRA, led by its still-popular 79-year-old founder, Victor Raul Haya de la Torre. One explanation may be Haya's continuing ability to draw large crowds whenever he makes a public address. Also, APRA has been able to attract the support of large numbers of young people, a feat that has eluded the military government.

The government would like to counter APRA's still widespread popularity, but its efforts thus far have been less than successful. The regime has used its own labor organization and SINAMOS to try to dilute APRA support among the peasants and lower class city dwellers. At the same time, lack of expertise and inter-service rivalries have hampered any moves by the government to establish its own political party. The government has made repeated attempts to gain the support of organized labor by offering compromise wage settlements and by appealing to workers' "revolutionary instincts." Nevertheless, individual labor groups have often opposed the

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regime when it has failed to satisfy their bread-and-butter demands.

### The Regime's Programs

Probably the most important and far-reaching plan of action yet instituted is the social property program, begun last May after a year of public scrutiny and criticism. Through a complicated bureaucratic mechanism, the government hopes eventually to transfer control of large numbers of businesses to worker-dominated groups. The "social property enterprises" thus formed, at least initially with government seed money, will in turn channel profits or "surpluses" into a fund for other enterprises. According to the decree law, every worker who participates in any social property enterprise will be a part owner of all others. At all times, however, it appears that the government will maintain a decisive—if camouflaged—voice in establishing, running, and, if necessary, terminating each enterprise. At least some of the theory behind this system derived from a study of the Yugoslav cooperatives.

The government has also developed two other mechanisms through which it intends to shift most economic power away from the oligarchs and private investors, and place it in the hands of the workers and the state. These are "industrial communities" and "basic industries." The government has allowed private individuals to maintain control of the smaller firms, at least for the time being. Notwithstanding these restrictive measures, some private businesses continue to make substantial profits.

As outlined in the so-called Inca Plan made public by President Velasco on July 28, the military envisages additional restructuring of virtually every phase of Peruvian life, including education, transportation, housing, and the judicial system. Although the plan—which Velasco claims was formulated prior to the 1968 take-over—is noticeably vague, the regime already has nationalized the important fishmeal and cement industries, begun a wide-ranging program of agrarian reform, and severely restricted or eradicated foreign investment in many areas heretofore heavily supported by outside capital. Indeed, the first major

### Signing compensation agreement



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step taken by the military government was the expropriation of the US-owned International Petroleum Company. And, on January 1, 1974, the government nationalized the huge, US-owned Cerro de Pasco mining complex.

This concern for "Peruvianizing" the nation's economy, however, has been tempered by the realization that Peru needs foreign loans and investment. This is particularly so in the exploitation of natural resources. Thus, foreign private investment is welcomed in certain instances, with restrictions that are somewhat more stringent than those adopted by the Andean Group. The government has just reached an agreement with a number of foreign investors to ensure the development of the large Cuajone copper reserves in the south, and it has obtained a substantial Japanese loan to construct an oil pipeline across the Andes.

It was this concern for continued investment that prompted Peru's leaders to reach a com-



**Velasco and Castro**

promise with US negotiators last spring, whereby Peru agreed to pay \$150 million in compensation for all US-owned businesses that had been nationalized since 1968. This removed the major irritant in US-Peruvian relations and has made subsequent talks on Eximbank loans and possible weapons purchases more cordial. The prospect of further nationalization of US-owned companies, such as Marcona Mining, is slight at present, but the possibility remains. Lima at any time may decide that the risks of another chill in relations with Washington are worthwhile if the political gains and the chances for other foreign investment outweigh any adverse economic effects.

### **Foreign Policy**

The basic thrust of Peru's foreign policy since 1968 has been and is likely to remain strongly nationalistic and identified with the non-aligned movement. The tenor of US-Peruvian relations, however, would probably become more strained if a radical such as General Graham were to succeed Velasco. General Morales Bermudez, on the other hand, could be expected to follow a more friendly path in relations with Washington.

At the same time, if serious snags develop in particular bilateral negotiations, such as arms sales or restructuring the OAS, Lima would probably not hesitate to risk yet another round of strained relations to assert its independent foreign policy stance.

Although Allende's ouster in Chile has made the Peruvian government stand out as the most radical in South America—causing some concern in Lima—Peru's nonaligned rhetoric and espousal of Third World unity has not wavered. Lima has been in the forefront of those less-developed countries advocating economic unity against the super powers and has taken the lead in calling for changes in the inter-American system to lessen US influence and incorporate the concept of "economic aggression" into the OAS charter. These policies are sure to continue after Velasco's departure, although the tone will vary depending on who succeeds him.

Contacts with Cuba, which have developed rapidly since diplomatic and trade relations were

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re-established in July 1972, can be expected to become even more prominent if Graham becomes president, but will remain an important element of Lima's policies regardless of Velasco's successor. Several top military leaders maintain close ties with their Cuban counterparts and would like to see these contacts expanded.

Relations with the Soviet Union, China, and Eastern Europe have also moved forward under Velasco's leadership, primarily as a means of asserting Peru's independence. Along these same lines, in international forums Peru has supported representatives from "liberation" movements in the less-developed countries of Asia and Africa.

Aside from political considerations, Peru has derived some tangible economic benefits from its association with the Communist countries—credits, fisheries cooperation, and port construction. In the case of the Soviet Union, however, Peruvian leaders resent what they view as foot-dragging by Moscow in matters of economic assistance. The best example concerns Soviet assistance in developing the giant Olmos River hydro-electric project. Several feasibility studies have been completed in the last five years but credits for construction have not been advanced.

In fact, most Peruvian leaders remain suspicious of Soviet motives and are reluctant to allow more than a minimal number of advisers and technicians into the country. For instance, although Peru has accepted some 14 Soviet tank instructors, it reportedly has balked at allowing 250 Soviet technicians to enter the country to conduct yet another feasibility study of the Olmos project.

The Velasco government has been willing to accept Soviet offers whenever they appeared to be the most—or only—viable economic alternative, as when Lima purchased an estimated 150 or more T-55 medium tanks. The first tanks arrived late last year, and as many as 120 may now be in Peru. President Velasco decided to accept the long-standing Soviet offer after extensive study made it apparent that sufficient numbers of comparable US or European tanks were not available. While the Peruvians reportedly have

experienced some problems in learning to operate the tanks, they are considering other Soviet offers, including patrol boats and surface-to-air missiles.

Arms procurement has become an important facet of Peru's foreign policy and is likely to remain so. In addition to the Soviet tanks, Peru has accepted delivery of 65 105-mm. towed howitzers from Yugoslavia. Lima also is awaiting delivery of additional Mirage jets from France and assorted ground, air, and naval weapons from other Western suppliers. The country's military leaders feel a genuine need to modernize and expand their forces as well as a desire to maintain them as one of Latin America's best-equipped. Also of considerable importance to Peru is the possibility of a conflict with Chile.

Peruvian military doctrine traditionally has called for a war with Chile to regain territories lost in the War of the Pacific (1879-83). Revanchist sentiments have become more pronounced since the military took power in Chile last September. Some leaders in Lima apparently fear that Chile under military rule will be able to narrow the "arms gap," which now favors Peru, long before 1979—the centenary of the war and the date by which the Peruvian military believes the "disgrace" of the last century must be



*Soviet-built T-55 tanks on parade*

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corrected. Also, some top Peruvian officers reportedly fear that Chile may provoke a conflict with Peru in order to relieve domestic pressures being exerted on that regime.

Both Peru and Chile have noted publicly that bilateral relations are "normal" and that any talk of hostilities is unfounded. Despite such maneuvering, and despite the fact that chances of deliberate hostilities in the next year or two are not great, Peru will press ahead with its arms procurement program and plans to upgrade its military posture. Already, a large number of the

army's T-55 tanks have been stationed near the Chilean border.

Peru's sense of isolation as the area's most radical government is also linked to concern over alleged Brazilian plans to seek Pacific coast territory through Peru. These fears have prompted the army to implement a long-term military expansion program in the eastern jungle. The feeling of isolation has been and will continue to be an important factor affecting the domestic policies of the Velasco government. [REDACTED]

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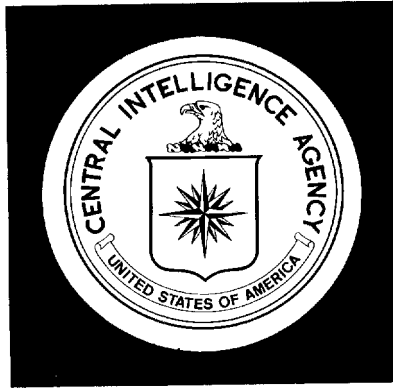
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# Weekly Summary

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# CYPRUS

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The talks between Greek Cypriot leader Clerides and Turkish Cypriot leader Denktash received a setback this week following the discovery of a mass grave of Turkish Cypriot villagers. The apparent massacre could revive pressures on Turkish leaders to "liberate" those Turkish Cypriots still in the Greek Cypriot - controlled sector of the island. The prospects for a negotiated settlement could also be complicated by disunity in the Greek Cypriot community as well as in Athens and Ankara.

and would probably settle for a less substantial or even token pullback of Turkish forces.

Thus far, the Turks appear unwilling to make any concessions in order to get negotiations under way. They appear instead, to see the question of refugees and military withdrawal as chips to be played once talks resume. They are unlikely, however, to make any major concessions. A Turkish Cypriot leader told the US ambassador in Nicosia this week that plans were under way to declare an "autonomous Turkish wing of a federative Cypriot state" within the "next few days or weeks." He said Turkish Cypriots would settle for 33 percent of the island.

The second in a planned series of discussions between Clerides and Denktash scheduled for September 2 was postponed at Denktash's insistence because of the discovery of the mass grave near Famagusta. Turkish Cypriots also claim that another such grave exists in a Greek-controlled area near Limassol.

On the Greek Cypriot side of the island, the attempted assassination on August 30 of a leftist maverick and Makarios confidant, Vassos Lyssaridis, and the killing of his party's youth group leader by suspected EOKA-B gunmen will further complicate Clerides' efforts to build a political base that could enable him to consent to a political settlement. While Lyssaridis implored his followers not to take reprisals, the attempt on his life and the murder of the popular youth group leader could spark further violence among extremist groups within the Greek Cypriot community.

Speaking at a press conference on September 3, Turkish Prime Minister Ecevit warned that Turkey "will be forced to take effective measures" if massacres or threats of massacres of Turkish Cypriots in Greek-controlled areas continue, or if Turkish Cypriots living in those areas are forced to live as prisoners.

## Developments in Greece

In Greece, Prime Minister Karamanlis' political honeymoon appears to have ended earlier this week with the formation by Andreas Papandreou of a new leftist party alternately referred to as the Panhellenic Socialist Movement and the Progressive Democratic Front. Papandreou is expected to be the principal challenger to Karamanlis' position. The leftist leader criticized the Karamanlis government for moving too slowly against the country's former military rulers and for failing to purge their supporters from the government. He said the principal aims of his party are the creation of a state free from foreign intervention and control as well as the socialist transformation of the country. He also called for Greece's complete

The publicity given to the massacres came at a time when Greek and Greek Cypriot leaders appeared to show some flexibility in their requirements for the reopening of negotiations. Greek Prime Minister Karamanlis seems to have dropped his demand that Turkish troops on Cyprus withdraw to positions held on August 9 prior to the second round of fighting. Karamanlis and Clerides also seem prepared to accept a federation of the two Cypriot communities. They now seem to be concentrating on the return of Greek Cypriot refugees to their homes, especially in Famagusta,

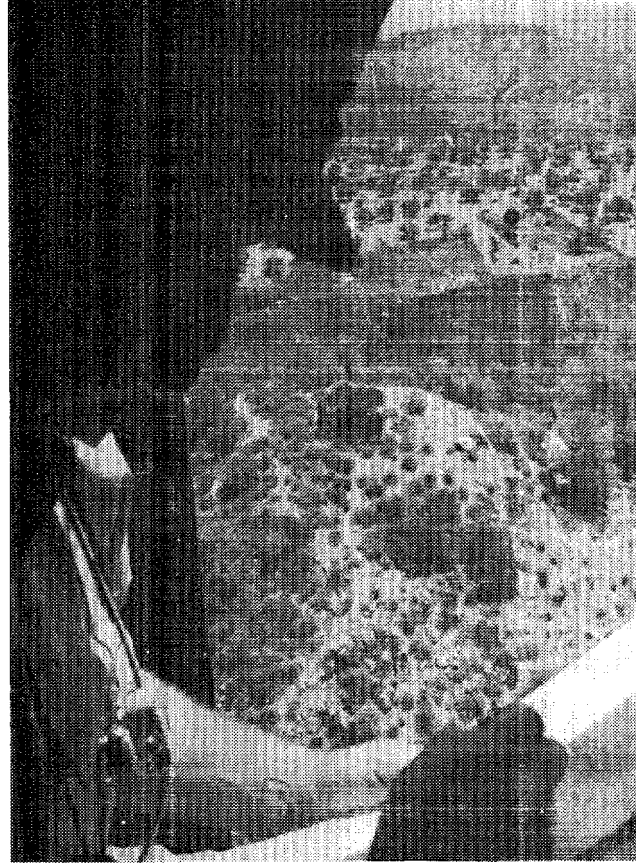
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break from NATO in favor of an <sup>(Not Sourced)</sup> "active, independent" foreign policy.

Earlier, Prime Minister Karamanlis, in a wide-ranging speech before a huge welcoming crowd in Thessaloniki, reaffirmed his decision to withdraw militarily from NATO, but added that Greece would not break its "political and spiritual ties to Europe." He also questioned the US role in the events surrounding the Turkish invasion of Cyprus, but placed primary responsibility on the junta that preceded him. The prime minister defended himself against "go slow" charges, saying it was impossible "to undo within a month what has been done within seven years of military rule." Karamanlis called on the nation, especially the press, to exhibit political maturity in this time of national crisis. Karamanlis said he would be able to announce a date for national elections in a time "much shorter than expected."

#### Frictions in Ankara

In Ankara, there were signs of growing friction within the coalition government of Prime Minister Ecevit. Ecevit held a press conference on September 3 during which he seemed to concede some difficulties with his right-wing minority partner, but insisted that there was a unity of views regarding Cyprus. Two days later, however, deputy Minister Erbakan, who heads Ecevit's junior coalition partner, accused Ecevit of making statements that harmed Turkey at a time when the Cyprus crisis made unity essential.



UN officer checking lines

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#### Military Developments

The military situation on Cyprus remains tense. Over the past week, Turkish forces continued to move slowly forward beyond the cease-fire lines. Regular Turkish troops inched south of the "green line" in Nicosia and near the British base at Dhekelia on the southeast coast. In addition, regular army forces and Turkish Cypriots consolidated their position on the northwest coast. By mid-week these forces were reported to have moved as far as Limnitis, and UN observers believed that the Turks may be planning to take Kokkina as well.

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### SOUTH VIETNAM: WORRIES ABOUT THE WAR

10 [Concern is growing in Saigon over its ability to contain increased Communist attacks in the face of reduced US aid. While some South Vietnamese commanders remain satisfied they can handle the present step-up in fighting, they are less sure about the longer term, especially if the Communists launch an offensive sometime next year.]

11 [Fairly serious reductions already have been ordered in aircraft and ammunition usage. Combat sorties and reconnaissance missions have been cut by approximately 50 percent, and more reductions are planned.] This has led several commanders to request approval to evacuate outposts and forward positions that can only be supplied by helicopter or air drop. The commander of the region surrounding Saigon wants to take his troops out of several such locations, including the provincial capital of An Loc, which served as the bulwark of government defense efforts during the 1972 offensive.

8 [While some field and regional commanders single out the reductions as the main reason for government problems on the battlefield, Saigon's Joint General Staff believes that the cutbacks can be handled without seriously jeopardizing the country's defenses. The General Staff appears to have President Thieu's support.]



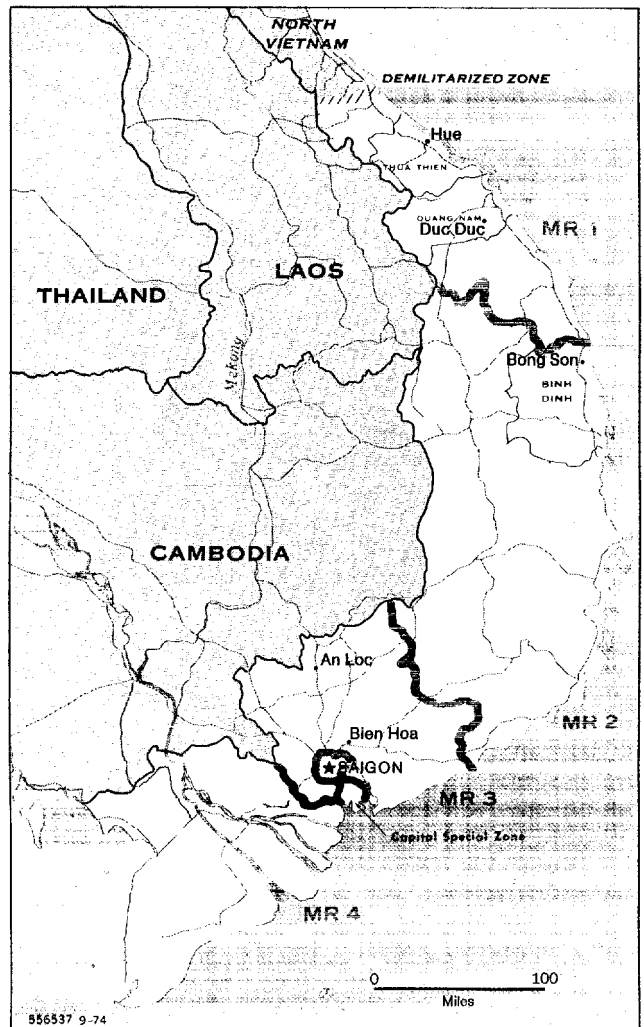
14 [Thieu is aware that his chances for getting the \$1 billion aid he wants from the US are slim, although he apparently still holds out hope that some of Congress' \$300-million cutback can be restored. By continuing to press for more restraint from his commanders, he is hoping to force them to become accustomed to fighting with only limited support from the US while at the same time creating a favorable image in the US by demonstrating he is making maximum use of the aid being given him.]

12 [Thieu cannot be getting much satisfaction from field reports on the recent fighting. The

Communists have pushed government units back in the northern provinces and near Saigon. Moreover, the Communists have demonstrated that they have ample military supplies to bring intense pressure on specific targets, and there are no signs they plan to reduce the current combat level anytime soon.]

### The Fighting Goes On

12 [Although the fighting decreased slightly in some sectors of the country this week, it is still



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heavy in the northern provinces. In Thua Thien Province, North Vietnamese troops attacked government positions west and south of Hue. A Communist artillery unit recently moved into this sector and is using 122-mm. guns to bombard government positions. In Quang Nam, the Communists are keeping the pressure on government forces with frequent shellings.

In Military Region 2, government commanders expect the Communists to resume the fighting in Binh Dinh Province. Several enemy units have shifted toward the coast near Bong Son, and aerial observers have spotted Communist artillery positions nearby. Saigon's forces have been realigned to meet the threat in this area.

Elsewhere in the country, combat has been relatively light. In Military Region 3, government troops are trying to push Communist units back in order to stave off shelling attacks on the large air base at Bien Hoa. The field commander, however, is not optimistic about his chances of retaking any territory. [redacted]

**CAMBODIA**

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**One Eye on the UN**

For the past few weeks, Cambodian government officials and military leaders alike have been

focusing on the coming battle at the UN General Assembly this fall. On the diplomatic circuit, Prime Minister Long Boret at midweek engineered a breakthrough in his efforts to win Arab support by announcing the establishment of full diplomatic relations with Jordan. In deference to Amman's sensitivities over Phnom Penh's ties with Israel, Boret agreed to transfer the Cambodian representative in Jerusalem to Tel Aviv. The Saudi Arabians, whose recognition Boret has also been seeking, have been pushing Phnom Penh to sever relations with Israel, but may drop this demand following Jordan's action.

Boret's Middle East travels have not gone unnoticed by Prince Sihanouk's "government." An Egyptian diplomat in Peking told a US official last week that Sihanouk's supporters are worried that Boret might succeed in eroding Arab support at the UN, and that they have therefore sought assurances of continued Egyptian backing. Sihanouk's representatives abroad have been concentrating on lobbying among African nations, but they can be expected to shift their attention to the Middle East soon, especially if Boret gains Saudi recognition.

**The Military Scene**

Cambodian army commanders have also been trying to put their best foot forward on the eve of the UN opening. In the Phnom Penh region, elements of three army divisions have launched a major operation into Communist-controlled territory between the Mekong and Bassac rivers southeast of the capital. Seasonal flooding is hampering the operation but the push has disrupted insurgent rocket-firing into Phnom Penh. In the countryside, government forces have launched successful forays near the provincial capitals of Pursat, Siem Reap, and Kampot.

The insurgents are concentrating on widespread attacks in rice-rich Battambang Province and on increasing pressure against government units along Route 4 in the southwest. [redacted]

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## LAOS: IN THE COMMUNIST OUTBACK

20 [Life in the "liberated zone" of Laos—the Communist-held Sam Neua area in the remote northeastern part of the country—is highly organized, tightly regimented, and dominated by a pervasive party organization patterned after the North Vietnamese model.]

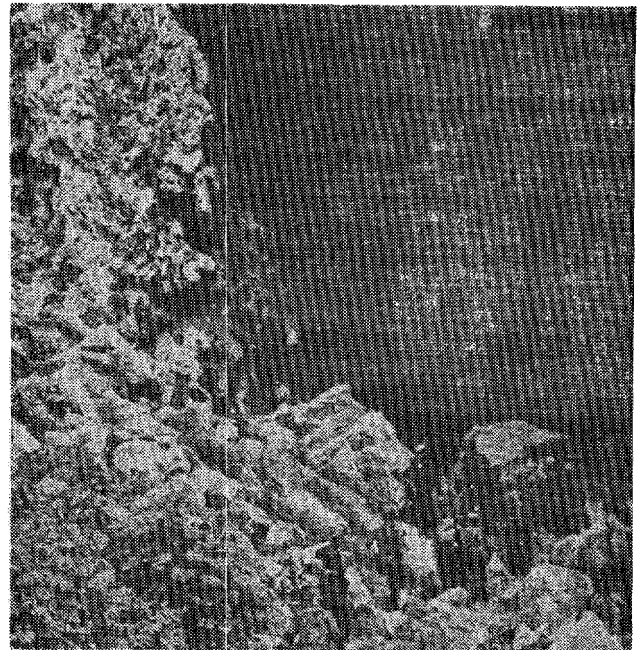
20 [So says Canberra's Ambassador Borthwick, who spent nearly a week earlier this summer touring Sam Neua and the new Lao Communist headquarters site at nearby Vieng Say. Although his visit was tightly controlled, the ambassador observed feverish reconstruction and road-building activity throughout both areas and was told that reconstruction is the most urgent problem in the "liberated zone." The Laotians claim to be doing as much as possible by themselves, but acknowledge that their manpower is limited and that Hanoi has been asked to send some North Vietnamese laborers to help out.]

20 [Borthwick's observations suggest a relaxation of the rigid war-time footing noted by the British, French, and Soviet ambassadors during their visits to the Sam Neua area early this year.] [Indeed, Borthwick's Central Committee host indicated that the party was encouraging the population to come out of the caves and rebuild the country.]

20 [Like his diplomatic predecessors, Borthwick found life in the Sam Neua area bleak and austere by Vientiane standards. In spite of their Spartan life, the people appeared adequately fed, clothed, and housed, and there are no signs of resistance to party direction.]

20 [No one has much money, but prices are controlled by the party and are stable. Although land is still privately held, there is only one outlet for surplus production—the party—and it is unclear whether the party buys or requisitions. The "liberated zone" earns little in exports, yet some people were sporting imported watches and transistor radios.]

21 [The ambassador's impressions of the primitiveness of the economy were corroborated by the coalition government's Pathet Lao deputy finance minister during a recent conversation with



Come out of the caves

the USAID director in Vientiane. The Communist minister indicated that the great differences in business administration and taxation between the Pathet Lao and the non-Communist zones precluded a combined national budget and an overall economic plan for the whole of Laos for some time.]

21 [The only form of taxation in the Pathet Lao zone, according to the minister, is a rice tax imposed as a percentage of the farmers' harvest. Civil servants, who receive compensation in the form of wages, rice, and other commodities, are not taxed. Although there are no private industries or significant commercial establishments, the minister acknowledged that there was some private enterprise in the liberated zone. Such entrepreneurs were "encouraged" by the party to market their goods at prices "more or less" comparable to those charged in Pathet Lao cooperative stores.]

20 [Ambassador Borthwick was struck by the apparent indifference to religion during his tour of the liberated zone. On joining the coalition government, the Pathet Lao had endorsed the importance of religion in national life and a Communist heads the coalition's Ministry of

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Religion. But in their own home territory, there are no active temples or monks, and no serious attempt is being made to restore damaged places of worship.]

U] Wherever the ambassador went, the cult of Souphanouvong was present. His portrait was prominently displayed in all official reception areas, either by itself or in concert with other legendary Communist heroes like Ho Chi Minh and Lenin.]

U] Neither of the two important Pathet Lao leaders who remain in Sam Neua—Central Committee chairman Kaysone Phomvihane or his deputy, Nouhak Phoumasavan—deigned to meet with Ambassador Borthwick. He did confer at length, however, with several lesser lights including General Phoune Sipraseuth. Although the conversations reflected the Central Committee's satisfaction with the new coalition arrangement, they also revealed the deep-seated distrust and suspicion that senior Pathet Lao officials continue to harbor toward the non-Communist side, the Thai, and the US.]

U] On the basis of these talks, and as the result of personal observations, Borthwick concluded that there will be no free movement between the two zones of Laos, much less any formal integration, for some time. In the ambassador's view, the administrative apparatus of the Lao Communists is still too fragile to be exposed to the worldly temptations of the "yet-to-be-liberated" zone.

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### ETHIOPIA: FADING DYNASTY

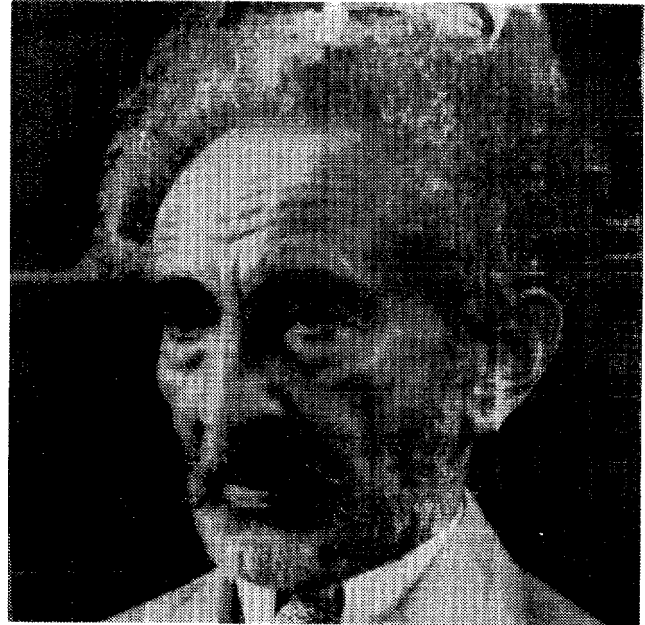
40 The Armed Forces Coordinating Committee continued this week to denigrate both Emperor Haile Selassie and the monarchy as an institution. Intensified public attacks on the Emperor in recent days, which were probably approved by the committee, suggest that the forces within the committee advocating the Emperor's removal and abolition of the monarchy—heretofore a radical minority—are gaining strength.

40 The beleaguered, 82-year-old Emperor probably has no delusions about his chances of regaining his shattered authority or prestige, and he apparently has done nothing to defend himself against the wide-ranging charges being leveled against him. Faced with mounting censure, he could choose to abdicate. The US embassy in London has been informed by a British official that one of the Emperor's grandsons made an approach this week through the British embassy in Addis Ababa to sound out the possibility of political asylum for Haile Selassie in the UK, where he found refuge during the Italian occupation of Ethiopia.

40 Last weekend, a well-organized group of students and unemployed youths demonstrated in front of the palace and elsewhere in the capital, demanding that the Emperor step down. Pamphlets and posters depicting him as indifferent to suffering drought victims also appeared in Addis Ababa, and he was reportedly spat on and cursed on his way to Sunday church services. The Ethiopian radio and press have begun to accuse him of salting away large sums of money in foreign banks.

40 Following last weekend's trouble, the committee issued a statement forbidding such demonstrations without its consent and ordered out armed police and military patrols. The committee probably fears that further demonstrations could quickly get out of hand or spark other incidents, particularly in rural areas where the committee suspects Haile Selassie may retain some support despite the recent denigration campaign.

40 The committee also announced that college and high school students should hold themselves ready for development and drought-relief



The Emperor

projects. The committee is probably concerned that the scheduled reopening of schools later this month could provide the volatile students with a greater opportunity to stir up trouble.

40 Although there is still some sentiment in the committee and elsewhere in the military for retaining the monarchy under a new emperor, the advocates of this course appear to be losing ground.

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40 In the event the committee decides to abolish the throne, it may first try to counter remaining pro-monarchist sentiment with an intensive media campaign depicting the military as saviors of the country. Laudatory treatment of the committee in the media has accelerated considerably in recent days.

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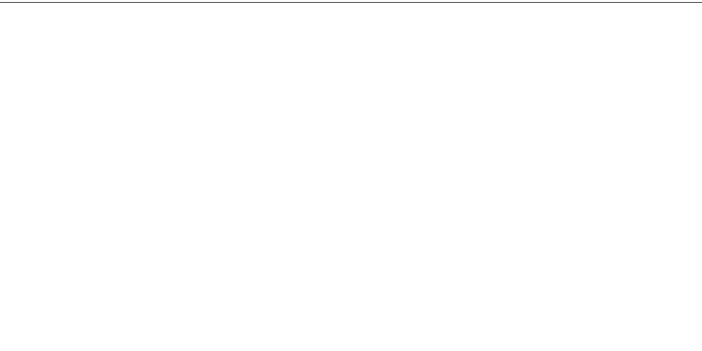
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**ISRAEL: RABIN TO VISIT US**

(61+62) (59)

Next week, Prime Minister Rabin will visit the US for the first time since he assumed office just over three months ago. Rabin's supporters and opponents alike will closely scrutinize the results for indications of the state of bilateral ties and prospects for further negotiations with the Arabs.

Many Israelis see the trip as an opportunity for their new leader to establish a good personal relationship with President Ford and to present Israel's case.



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The Israeli press over the past few weeks has frequently expressed suspicion that the US is forcing the pace of the negotiations at Israel's expense.

Rabin has stated on several occasions during the past months that Israel has little choice but to continue on the negotiation path if it wishes to avoid a new war.

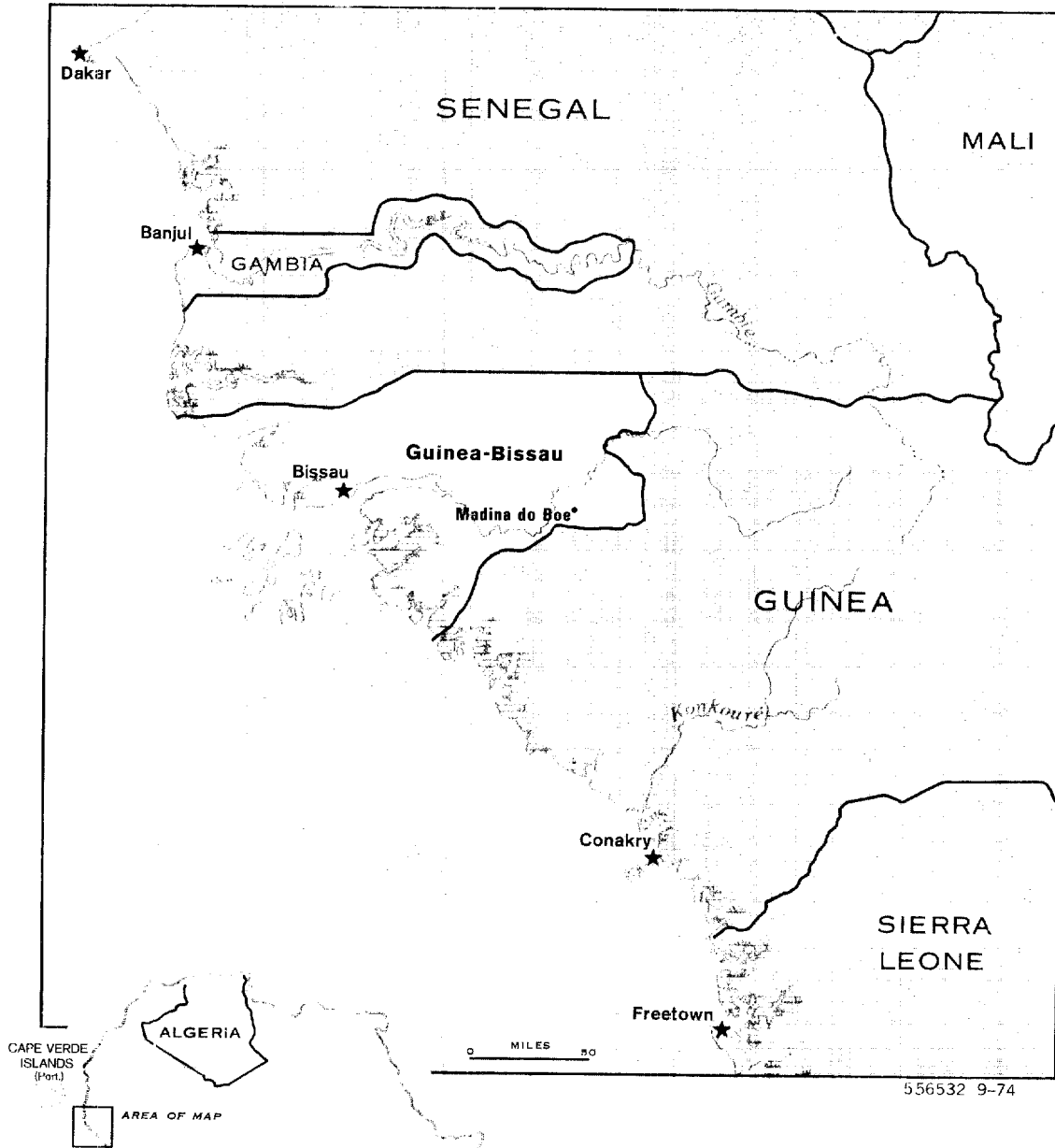


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Rabin firmly believes, however, that only a militarily strong Israel can afford to be flexible in the negotiations. He can be expected to argue forcefully for a large, long-term US commitment to provide Israel with the necessary military and economic aid, Tel Aviv's price for further negotiations.

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**GUINEA-BISSAU: FORMAL DEBUT**

67 Portuguese Guinea, the oldest and poorest of Portugal's African territories, will gain Lisbon's official recognition as the independent Republic of Guinea-Bissau on September 10. The formal transfer of authority will end over 500 years of Portuguese rule and more than a decade of armed insurgency. The independent government will face a formidable array of problems. Even with massive assistance from Lisbon and other foreign supporters, it faces an unsteady future.7

68 The exact form the new government will take is not yet clear. The structure established by the rebels a year ago when they unilaterally proclaimed the territory's independence consists of: 69 a 120-member National Popular Assembly, which functions as a policy-making body; a 15-member Council of State; and a cabinet of seven commissars and their deputies. The rebels' African Party for the Independence of Portuguese Guinea and Cape Verde is the only political organization and is expected to dominate the government; party secretary general Aristides Pereira will thus be the country's top leader7

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68 [redacted] the republic's official capital will be located at Madina do Boe, the small southeastern town where the rebels proclaimed their government. Such a designation would presumably be for symbolic reasons only, however, because Madina is too isolated. Bissau is likely to continue as the administrative and economic center7

69 On its admission to the UN, expected soon after the General Assembly convenes on September 17, Guinea-Bissau will rank among the world organization's poorest and least developed members. Portugal expects to contribute heavily to the country's development and probably will leave behind large numbers of technicians, educators, and medical personnel. In fact, the republic's economy is likely to remain basically tied

to Lisbon for some time to come, although the nationalist leadership will want to modify the near monopoly long enjoyed by the Portuguese7

69 The leaders of the new state could also be in for some stormy political weather. The bulk of the government's leadership is made up of mulattoes from the Cape Verde Islands, although the vast majority in the fighting ranks of the victorious rebel movement are blacks from Guinea-Bissau. In the past, this distinction has caused friction between the political and military wings of the party, but the leaders so far have been able to smooth this over. With independence, however, black resentment of Cape Verdeans in positions of leadership could become a major issue. Even among non-insurgents, there is resentment against Cape Verdeans, stemming from Portugal's reliance on the islanders to help colonize and administer Portuguese Guinea7

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*INDEPENDENCE ENDS 500 YEARS OF PORTUGUESE RULE AND MORE THAN A DECADE OF ARMED INSURGENCY.*

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69 Officials of the new government have publicly affirmed a nonaligned foreign policy. Guinea-Bissau is likely to have close relations with Senegal and Algeria, two countries that served as intermediaries during negotiations with Lisbon. The course of relations with neighboring Guinea, which was the rebel movement's staunchest African backer over the years, is less predictable. Relations have been somewhat strained in recent months, largely because Guinean President Sekou Toure did not approve the rebels' decision to negotiate with Lisbon after the April coup. The USSR and Cuba will enjoy some degree of special favor because of their extensive military assistance, but rebel leaders have insisted that they intend to remain free of Communist influence.

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**INDIA-SIKKIM: TOWARD MERGER**

70 [India amended its constitution this week to give its strategically located protectorate of Sikkim representation in parliament as an associate state of the Indian Union. New Delhi's action was the latest in a series of steps it has taken to tighten control over Sikkim after political unrest erupted there last year. The end result seems likely to be the complete absorption of the protectorate.]

71 [India fears that prolonged instability in any of the three Himalayan buffer states (Sikkim, Nepal, Bhutan) would create a vulnerability that China might exploit. Such a situation seemed to be shaping up in Sikkim last year when leaders of the ethnic Nepalese majority of the population sought to eliminate economic and political practices that favored the ethnic minority, represented by the hereditary ruler, the Chogyal, and to strengthen ties with India. The Chogyal reluctantly agreed to accept a political compromise arranged by New Delhi after he had to ask for Indian troops to bring anti-royalist demonstrations under control.]

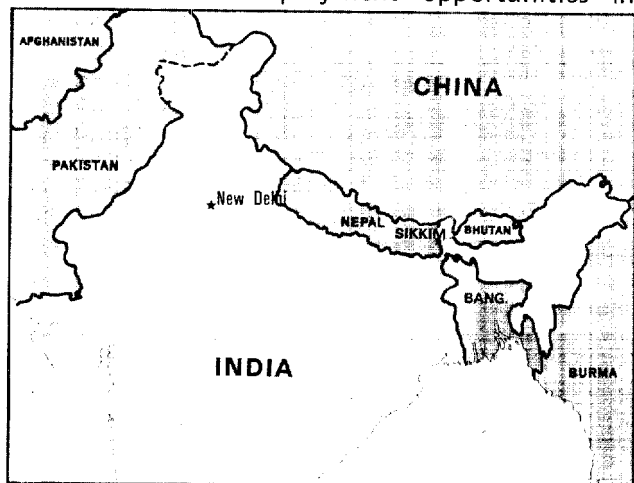
71 [A new constitution, drafted by India, went into effect in Sikkim last July. It reduces the Chogyal to a figurehead, provides for a legislative body elected on a one-man, one-vote basis, and establishes India's direct control over internal matters. New Delhi has also agreed to strengthen economic ties and to provide Sikkimese with educational and employment opportunities in



**The Chogyal**

India. New Delhi retains exclusive responsibility for Sikkim's defense, communications, and foreign affairs, which was established under the 1950 Indo-Sikkim treaty.]

71 [India's latest move has been denounced by the 51-year-old Chogyal in a desperate bid for international support. In the past, he has threatened to abdicate in the face of Indian pressure, but New Delhi probably will continue to encourage him to remain as titular head in hopes of muting foreign criticism of its "take-over.".]



71 [Although New Delhi probably anticipated some Chinese criticism of its action, the comment in *People's Daily* this week was Peking's strongest attack on India in some time. The commentary not only includes a direct attack on Prime Minister Gandhi, but it makes clear that Peking does not plan an early rapprochement with India.]

70 [Officials in Nepal, who are customarily reluctant to comment on Indian moves in Sikkim, were also sharply critical of New Delhi this week. Anti-India student demonstrations in Kathmandu appeared to have government approval, suggesting that the "rape of Sikkim" may become a contentious issue between India and Nepal.]

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**FEDAYEEN: LOOKING TO THE UN**

66 [The Palestine Liberation Organization has apparently decided to try to raise the Palestinian issue at the UN General Assembly session that begins later this month. At the same time, the fedayeen grouping is opposing Egyptian calls for a compromise of the Jordan-PLO dispute in order to achieve a common Arab policy on the Middle East peace negotiations.]

63 [Early this week, the Arab League's foreign ministers' council approved a request by PLO chairman Yasir Arafat to place the Palestinian question on the agenda of the General Assembly.]  
66 [According to the US embassy in Beirut, the PLO has apparently set its sights on gaining full observer status at the UN. It may also seek General Assembly support for a resolution that would recognize the PLO as the "sole" representative of all Palestinians, although this controversial issue was apparently not raised at the Arab League meeting. The Palestinians are referred to only as refugees in Security Council Resolution 242 of 1967.]

66 [During his visit to Moscow last month, Arafat may have been encouraged to press the Palestinian case at the UN. The Soviets reportedly indicated that they would be disposed to support such a move. In any case, Arafat's initiative is in line with his wide-ranging efforts to seek maximum international support for the Palestinian cause in order to buttress the PLO's claim to a seat at the Geneva peace conference. Official recognition of the PLO within the UN would also help Arafat resist pressure from fedayeen radicals who oppose Palestinian participation in the peace negotiations.]

66 [Although the other Arabs are supporting the move to give the PLO observer status at the UN, any move by the PLO to press for international recognition as the Palestinians' "sole" representative could force the Jordanians out of the Geneva peace talks. That would undermine Egypt's

efforts to achieve a compromise allowing both the Jordanians and the Palestinians to negotiate there.]

64 [Last week, the PLO executive committee reportedly voted to reject, at least for the time being, an Egyptian invitation to attend a tripartite Egyptian-Syrian-Palestinian conference that was to focus on reconciling PLO and Jordanian positions prior to the next phase of the peace talks. PLO representatives reportedly told the Egyptians that their decision was final unless President Sadat retracted his support of King Husayn's right to speak for the Palestinians living in Jordan and promised full support for the inscription of the Palestinian issue on the General Assembly agenda.]

*THE PLO OPPOSES COMPROMISE WITH JORDAN AND SEEKS UN RECOGNITION AS SOLE SPOKESMAN OF PALESTINIANS.*

66 [The PLO's move may be an attempt to force Sadat to restore complete support for the organization, a ploy that seems unlikely to succeed. Although Sadat has agreed to back the Palestinians' case at the UN, he has also reiterated his view that the PLO is not the sole representative of the Palestinians. Indeed, the Egyptian President appears to be on the verge of telling the PLO, on a take it or leave it basis, that the organization must allow Jordan to take the lead in negotiating the return of the West Bank.]

65 [If Sadat does not waver, the PLO might reverse its position. Early this week, Foreign Minister Fahmi remained optimistic that the tripartite meeting would take place, although he acknowledged that the PLO was still being difficult. If the PLO remains firm, Sadat's next move might be to try to convene a conference of Egypt, Syria, and Jordan aimed at working out a negotiating position that could then be presented to the PLO. Syria, however, would find it difficult to go along if the Palestinians remain adamant.]

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**USSR-US: TRADE DEFICIT REDUCED**

(73)  
 US statistics for the first half of this year indicate that Moscow's trade deficit with the US in 1974 will be less than half of the record \$1 billion set last year. Soviet imports from the US in the first six months totaled \$316 million, down by 55 percent compared with the same period in 1973. Exports to the US climbed to \$188 million, more than double the amount last year.

A \$400-million decline in purchases of US agricultural products was responsible for the fall in imports; purchases of machinery and equipment showed no change from the 1973 rate. The increase in sales to the US, compared with the first half of 1973, was led by oil and oil products and platinum group metals. The greater value of petroleum sales was largely a result of higher prices.

The data for the first six months suggest that imports from the US for the year will fall short of the billion dollar mark, perhaps totaling \$800 million. With less than \$100 million in grain to be imported in the last half of 1974, Moscow's total

imports of agricultural products from the US probably will fall short of \$300 million. Imports of machinery and equipment are likely to be substantially higher in the second half of 1974 and may reach \$300-\$400 million for the year.

Sales to the US for the whole of 1974 will depend heavily on the volume and price of imports of oil and platinum group metals. A doubling of total exports to the US over the 1973 level seems likely—to roughly \$400 million.

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**SOVIET-US TRADE<sup>a/</sup>**  
 (Million US \$)

	Year 1973	First Half 1973	First Half 1974
<b>USSR Imports</b>	<b>1,187</b>	<b>694</b>	<b>316</b>
Grain	837	511	168
Soybeans	67	67	--
Machinery and equipment	204	74	102
Chemicals	17	9	11
Iron and Steel	14*	5	6
Other	48	28	29
<b>USSR Exports</b>	<b>214</b>	<b>87</b>	<b>188</b>
Oil and Oil products	76	18	67
Platinum and platinum group metals	75	43	83
Diamonds and other precious stones	17	7	6
Chrome ore	6	2	3
Nonferrous base metals	18	6	12
Other	22	11	17

<sup>a/</sup> US trade statistics.

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### DENMARK: GOVERNMENT TROUBLES



Hartling

77 [Denmark's minority government narrowly averted collapse last week for the third time this year. At issue was the crucial third and final stage of Prime Minister Hartling's proposed economic reform program designed to deal with Denmark's persistent problems of inflation, budgetary deficits, and balance-of-payments problems. Hartling can rely on the support of only his Moderate Liberal Party, which controls 22 of parliament's 179 seats. The new legislation is due in parliament on September 12]

77 [Hartling consulted leaders of all parties last weekend after his talks with the key opposition group, the powerful Social Democrats, broke down. The Social Democrats apparently balked at Hartling's intention to pare government spending by about \$800 million, mostly in social and educational areas.]

78 [The Social Democrats regard cuts of this magnitude as unwise, especially during the current economic slowdown, and they want to reduce the cuts by half. The Social Democrats also favor cuts in government spending on defense and agriculture, but Hartling is reluctant to take this step. The Prime Minister rebuffed a Social Democratic proposal last week to cut defense spending by about five percent. The proposed reduction would have affected Denmark's NATO commitments, in addition to breaching a four-party agreement reached in 1973 to maintain defense spending at current levels through 1977]

79 [In his war of nerves with the opposition, Hartling has not hesitated to use the threat of resignation to exploit the general reluctance of all leaders to hold early elections. At the same time, he has indicated that he does not relish the prospect of calling new elections and is prepared to compromise with the non-socialist opposition. This would entail giving up a key tax reform, however, and risking a tough round of wage negotiations with labor this fall. Another option would be to bring the Social Democrats into a center-left coalition, but this would diminish the Moderate Liberal role and shift the direction of reform.]

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**OAS: FACING THE CUBA QUESTION**

90] Removal of the OAS sanctions against Cuba within the next month or two is accepted as a foregone conclusion by Latin American governments on both sides of the issue. Only the precise timing and manner remain in doubt. This week or next, Costa Rica, Venezuela, and Colombia will submit a proposal to the OAS on how to proceed. Most likely, an OAS forum will first take formal cognizance of a "changed situation" with respect to Cuba and then set a date for the OAS foreign ministers, in their capacity as the executive body of the Rio Treaty, to vote on terminating the ten-year-old sanctions]

91] Panama's recent defection from the ranks of members still observing the sanctions has increased the sense of urgency to restore the integrity of the Rio Treaty and the OAS. Seven of the 23 members now have diplomatic links with Cuba, and a strong majority clearly wants to establish them. Given these political realities, even the members still hostile to the Castro regime see little value in holding to the crumbled sanctions policy. Governmental changes in Washington, moreover, have heightened concern that the US will alter its Cuban policy and leave the few dedicated anti-Castro governments diplomatically isolated]

92] As for Cuba, Havana has a legalistic perception of the current sanctions dilemma and would view a termination of the sanctions as an unjustifiable confirmation of their original legality. For this reason, some OAS members—possibly at Cuba's urging—have cautioned against the creation of a committee to determine whether Havana is continuing to "export revolution"; these countries would prefer to avoid holding Cuba up to judgment and would rather base the elimination of the sanctions on changed world conditions. For their part, the Cubans, despite Fidel Castro's stated interest in a reconciliation with the US, want no part of the OAS. They reject it as a tool of the US for suppressing Latin America, and they will continue to work toward its destruction]

92] How the resolution of the Cuba question plays itself out will have varying effects on the new dialogue between the US and the Latin Americans—an exchange very much in the testing stage. Those governments advocating a new attitude toward Cuba would be gratified to see the US bend to their pressure; if the US maintains unyielding support of the sanctions, they would gravely doubt its flexibility on other issues. The countries that have supported the sanctions along with the US, on the other hand, are more anxious to test US willingness to consult and would be slow to forgive a surprise US change of heart]

92] Nevertheless, all the governments would be pleased to have the OAS rid of the contentious sanctions problem so that other pending questions could be grappled with. Many practical matters of common concern, most of them broad economic issues, are under study by inter-American committees. A number of large political questions also remain unanswered: Is the OAS—particularly an OAS without Cuba—a useful instrument for inter-American cooperation? Is the informal device of meetings of foreign ministers a more serviceable vehicle for the dialogue? Do the Latin Americans need or want a separate council excluding the US?]

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*REMOVAL OF THE SANCTIONS IS NOW A MATTER OF TIMING AND METHOD.*

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92] All these and other questions are in debate and under examination, with at least some chance that movement toward solving them will occur next year. Various reports and recommendations are scheduled for the ministers' meeting now set for March 1975, to be followed by the OAS General Assembly. Next spring, too, a new secretary general of the OAS must be elected, a task that will help to define what kind of future the Latin Americans see for the inter-American system.

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**CHILE: ANNIVERSARY APPROACHES**

93 Concern that leftists may try to use violence to mark the first anniversary of President Allende's overthrow on September 11 has caused the government to tighten security.

93 Security forces are especially concerned about the safety of government leaders during the anniversary and the subsequent national holiday on September 18-19.

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94 [Redacted]

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97 Mass arrests of "criminal elements"—undoubtedly aimed in part at ferreting out leftists—began in mid-July and appear to be intensifying as the anniversary approaches. Moreover, there apparently have been some recent incidents of local violations of the government's official policy against summary executions of prisoners.

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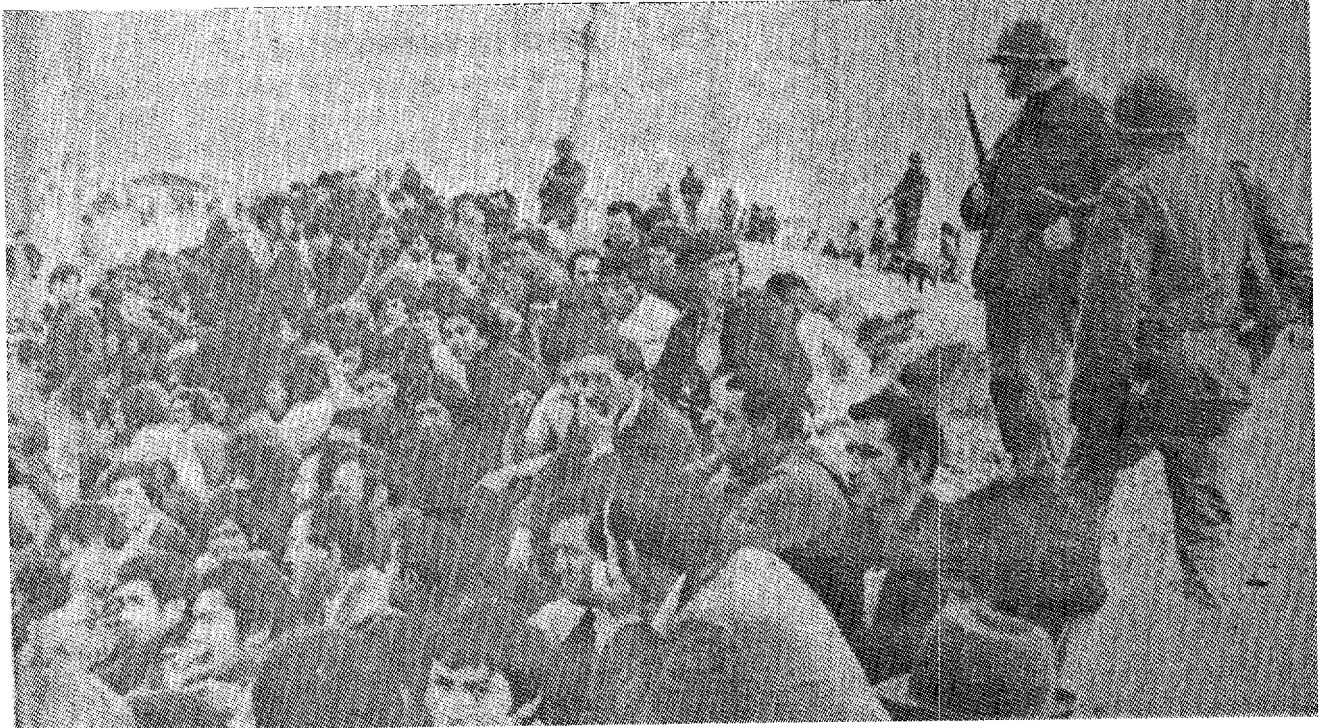
announce modification of the year-old states of war and siege, as well as to make a major gesture in the area of human rights. Pinochet announced no specific initiatives during a two-hour press conference this week, although he did note that the government was on the verge of deciding what to do with the Allende cabinet officers and leftist party leaders it has held since the coup.

97 In previous statements, Pinochet has ruled out any general amnesty but has disclosed that the government is studying the "commutation or reduction of sentences" of persons already tried and convicted of "lesser crimes." His conciliatory reply to a recent human rights appeal from religious leaders is another indication that some government move is in the works. The announcement might be included in Pinochet's speech on September 11, but it could be delayed until the national holiday observances the following week.

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97 There has been considerable speculation about government plans to use the occasion to

**Troops stand guard over suspects**



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**SECRET****INTERNATIONAL****PAYING THE OIL BILLS**

(98+99)

Japan, the UK, and Italy have been struggling to meet oil import bills that will total nearly \$35 billion this year. The UK and Italy have arranged adequate financing for 1974, but will face increasing difficulties next year. Japan is reducing its current account deficit and should have little difficulty financing the remainder.

Japan so far has coped with the \$14-billion increase in its annual oil costs without massive public borrowing abroad. In response to the problem, Tokyo has:

- tightened the monetary and fiscal policy another notch to hold down import demand and free more goods for export;
- put direct limits on business investment;
- restricted energy consumption in industry;
- discouraged investment abroad except in projects needed to assure supplies of raw materials, particularly fuel.

As a result of these measures and the impact of the higher oil bill itself, gross national product and the volume of imports have fallen while exports have continued to increase sharply. Japan's surplus in non-oil trade soared to \$6.3 billion in the first six months of 1974, holding the current account deficit to \$5.7 billion. Long-term capital movements abroad were reduced to \$2.6 billion from \$5.5 billion in the last half of 1973. Short-term commercial bank borrowing not only financed the resulting \$8.3 billion deficit in the overall balance but also brought a \$1.2 billion increase in Japan's official reserves.

Japanese banks are finding it increasingly difficult to borrow short-term funds to cover longer term financing needs. Tokyo accordingly is now seeking medium-term loans in international

capital markets and from OPEC countries. Japan has recently arranged a \$1 billion, four-year loan from Saudi Arabia. Tokyo will probably seek further medium-term aid this year to avoid any substantial use of its reserves or an increase in its short-term debt.

The UK, unlike Japan, had a deficit in non-oil trade of \$2.4 billion in the first half of 1974, in addition to its oil bill of nearly \$4 billion. Britain's traditional surplus in service transactions limited the current account deficit to \$4.8 billion—\$1 billion less than Japan's.

To meet the deficit expected for 1974, public authorities and private firms arranged about \$4.7 billion in Eurodollar credits. Only \$1.7 billion had to be used in the first half. The remainder of the deficit was financed through other capital transfers from abroad, including sterling deposits by some oil producers and increases in sterling working balances of international oil companies.

Capital transfers from abroad, including those from loans already arranged, will provide Britain with ample financing for the rest of 1974. The UK, however, appears to be receiving a smaller share of oil-related capital flows now than earlier this year. If this situation continues, London will have to find alternative sources of funds, which could be difficult.

Italy has the most formidable payments problem of any major country. Its \$3.5 billion cost of oil in the first half of 1974 came on top of a deficit for non-oil trade and a substantial outflow of long-term capital, raising financing needs to \$6.3 billion.

To make the necessary payments in the first half, Italy borrowed about \$2.3 billion in the Eurodollar market, obtained \$1.9 billion in

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short-term credits from its EC partners, and drew down official reserves by \$1.1 billion. By the end of June, foreign exchange reserves had dwindled to just over \$1 billion.

Rome's medium-term credit arrangements will carry it through the rest of the year if the EC, as expected, grants a three-month extension on the \$1.9 billion short-term credit. A \$2 billion loan from West Germany, arranged last week, and Italy's credit position in the International Monetary Fund give Rome about \$3.5 billion in medium-term resources.

Italy must now look for funds to meet the expected needs of next year. Rome is nearing its limit for private credit. The use of gold as collateral in the West German loan has further prejudiced Italy's private credit position, since lenders would probably want a similar provision in any new private loan. The most likely source of new medium-term credit is through an EC-backed arrangement which Bonn will probably support. Now that West Germany has given direct help to Italy, Bonn is in a strong position to push for community acceptance of EC-wide action.

#### PROBLEMS AHEAD FOR LARGE TANKERS

[ The most striking development <sup>(100)</sup> in maritime petroleum transportation over the past five years has been the tremendous growth in the construction of very large crude carriers—tankers of 175,000 deadweight tons and up. First introduced in the latter half of the 1960s, these tankers now account for almost half of the world's total tanker tonnage, and will probably form about two thirds of the fleet by the late 1970s.

Tremendous economies are realizable in the construction of very large crude carriers, and a number of countries are preparing to build even larger tankers than the existing 500,000-ton ships. French yards are already building tankers in

excess of 500,000 tons; tankers up to 700,000 tons are on order. Spain is investing \$310 million in a new drydock at Cadiz capable of building 1-million-ton tankers. Japan has set up a joint government-business committee to study the construction, financial, and operational problems connected with these ships.

The explosive growth of very large crude carriers was encouraged by the closing of the Suez Canal in 1967 as well as the booming demand for Persian Gulf oil. The cost advantages of using larger ships have long been recognized. For example, as the size of a tanker increases from 50,000 tons to 250,000 tons, the cost of hauling a barrel of oil around Africa from the Persian Gulf to the US east coast falls by more than 50 percent.

Despite the large tankers' growing popularity, several trends are developing that cloud future prospects. The worldwide economic slowdown and high oil prices have slowed the growth of oil consumption at a time when new tanker capacity is entering service in record amounts. As a result, spot tanker rates have dropped to a fourth of their level just before the Arab-Israeli war in October 1973.

Some industry estimates indicate that there may be as much as 100 million tons of excess capacity by the late 1970s, putting added downward pressure both on rates and on new orders for large tankers. The oversupply problem will be aggravated by the reopening of the Suez Canal—expected in about a year—which could reduce tanker demand by about 10 percent. Arab production cutbacks will result in additional excess tanker capacity.

Other operational problems are inhibiting the growth of tanker size. Tankers of almost 500,000 tons, chartered out to haul Persian Gulf oil to Japan, cannot pass through the Strait of Malacca when fully loaded, and must detour

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1,200 miles via the Lombok Strait. <sup>(120)</sup> Port limitations also are a problem. Harbors in the US can only handle tankers of about 100,000 tons; Western Europe's are limited to about 250,000 tons. Only Japan is able to handle the real behemoths. In addition, fear of oil pollution or other catastrophies has encouraged opposition to port expansion and passage rights by some countries.

The planned build-up of refining capacity in the Middle East in the next ten years will also affect tanker demand. Smaller specialized vessels,

#### Conference delegates



rather than very large crude carriers, will be required to haul products to the consuming nations. Uncertainty in the world petroleum market and forecasts of huge tanker surpluses through the end of the 1970s are likely to cause a substantial shift toward smaller, more versatile tankers.]

#### WORLD POPULATION CONFERENCE

<sup>103</sup> The UN-sponsored World Population Conference in Bucharest wound up its work last week by adopting a plan of action that calls for:

- Reduction of birth rates in developing countries by 1985.

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- Greater dissemination of family planning advice and services.
- More assistance from developed to the less-developed nations.
- Improvement in the status of women.

102 [Family planning and improved status of women were the two dominant themes of the conference. The US delegation succeeded in introducing into the plan strong references to women's rights to equal participation in educational, social, economic, cultural, and political life. Delegations from the Third World—particularly Latin America and Africa—came close to sidetracking the conference in its opening days, arguing that it is futile to reduce population growth until there is a fundamental restructuring of society.]

102 [The conference was punctuated by sharp exchanges on some political issues. The Chinese attacked both the US and the USSR, but they made special mention of "social imperialism" and 103 "that super power which labels itself socialist."]

The Romanians won adoption of a sweeping resolution entitled "For a More Just World" that in effect expands on their pet ideas for the conduct of interstate relations.]

102 [Bucharest was instrumental in avoiding a floor fight over the potentially disruptive issue of seating representatives of the South Vietnamese Provisional Revolutionary Government. The Romanians had worked diligently before the conference to have the South Vietnamese Communists seated. Once their efforts failed, Bucharest apparently lobbied hard in support of the US position that the South Vietnamese Communists should not be present.]

102 [Although the Romanians proved to be good hosts, they could not avoid the temptation to needle the Soviets. They distributed brochures to the conference participants that contained uncomplimentary references to the transfer of Bessarabia and Northern Bukovina to the USSR in 1940, and further rankled their Soviet comrades by charging them full hotel prices instead of cut-rate "fraternal prices." ]

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