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Central Intelligence Agency



Washington, D.C. 20505

DIRECTORATE OF INTELLIGENCE

14 SEP 1983

MEMORANDUM FOR: Douglas P. Mulholland
Special Assistant to the Secretary for
National Security Affairs
Department of the Treasury

FROM :
Chief, International Finance Branch

SUBJECT : Treasury Request for LDC Political Assessments
for IMF/IBRD Meetings

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1. The attached country sheets respond to your request for brief political assessments of a number of key LDCs for use by Treasury officials preparing for the 27-30 September IMF/IBRD Annual Meeting. Discussions whittled the original 22 country list down to these 13:

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- | | | |
|-----------|----------|--------------|
| Algeria | India | Peru |
| Argentina | Mexico | Philippines |
| Brazil | Morocco | Saudi Arabia |
| Chile | Nigeria | |
| Egypt | Pakistan | |

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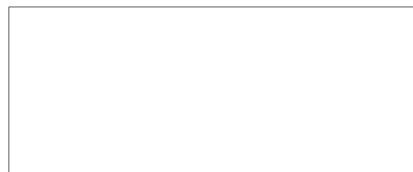
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Where appropriate, analysts have made specific references to the impact of LDCs' external financial problems on domestic political conditions.

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2. If you have any questions please call me

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Attachment:
Political Assessment of Key LDCs Attending
27-30 September IMF/IBRD Annual Meeting.
GI M 83-10227, September, 1983

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GI M 83-10227



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Political Assessment of Key LDCs Attending 27-30 September IMF-IBRD Annual Meeting

OGI/ECD/IF/ [redacted] 16Sept83

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Distribution:

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- 1- SA/DDCI
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- 1 - NIO/Economics
- 1 - D/ALA
- 1 - D/NESA
- 1 - D/OEA
- 1 - D/OGI
- 1 - Ch/ECD
- 2 - Ch/ECD [redacted]
- 1 - Ch/CPAS/ILS
- 8 - OGI/PS

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GI M 83-10227
September 1983

AlgeriaKey Domestic Issues

- o Algeria finds itself squeezed by the soft oil market; crude oil exports have dropped 75 percent since 1978 but are partially offset by expanded natural gas sales and higher gas prices.
- o The government has avoided the massive debt problems of other LDCs; this year, however, Algiers had to finance a SONATRACH project with a \$500 million loan on the Euromarket—the country's first substantial new borrowing since 1979.
- o The tight rein on borrowing has forced Algeria to draw down foreign exchange reserves from \$3.8 billion in 1980 to \$1.9 billion as of June 1983—about two and a half months of imports—and, according to press reports, to cut back on planned imports by at least \$1 billion for 1983.
- o Despite austerity measures and increased costs for consumer goods this year, we believe the Bendjedid regime enjoys public confidence. [redacted]

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Comment

In our judgment, President Chadli Bendjedid's authoritarian, non-aligned government is secure for the foreseeable future. He retains solid support among the armed forces and civilian technocrats, and he is probably more popular with the Algerian public than his two predecessors. The fragmented opposition—primarily doctrinaire leftists and Islamic fundamentalists—lacks effective leaders and organization. Some popular, non-revolutionary dissent occasionally is expressed by labor, students, or ethnic minority groups, but at present the government is addressing their grievances adequately. In any event, the security services would deal with any disorder firmly but peacefully, if possible. [redacted]

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The Algerian populace expect Bendjedid to alleviate Algeria's chronic unemployment and consumer shortages. Since 1980 he has redirected economic policy away from heavy industry and toward light industry, housing, and agriculture—areas directly affecting the average Algerian. A weakened market for oil, however, complicates this policy. Lower oil revenues have also forced the government to cut nonessential consumer imports such as autos and refrigerators. If the soft oil market and dwindling foreign exchange reserves force Bendjedid to implement further domestic belt-tightening, public dissatisfaction with his government may emerge. Alternatively Algiers may increase its foreign borrowing, but we expect it will seek such financing with considerable reluctance and judiciously. Bendjedid thus faces increasing difficulty in balancing consumer and development needs against diminished income, but we do not believe these problems constitute a threat to his regime. [redacted]

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In the longer term, Algeria will have difficulty offsetting declining oil reserves with increased production from its enormous gas reserves. In the event that gas contracts and expansion of production are not forthcoming, Algeria will have to cut imports and investments further and step up its foreign borrowing. [redacted]

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[REDACTED]

Argentina

Key Domestic Issues

- o Civilians will assume power after seven years of military rule following the 30 October general elections.
- o Economically, Argentina is experiencing a modest recovery from the chaos set in motion by the Falklands crisis, but the stabilization program is threatened by recent concessions aimed at placating labor.
- o The dispute over the Falklands with the UK still dominates Argentine diplomatic activity. [REDACTED]

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Comment

The preelectoral period has been characterized by continued tensions within the military over the course of the transition, the protection of its institutional interests, and the role of the services in the new government. Organized labor has been restive during the past months as unions work to wrest wage and other concessions before the new government takes power. At this juncture, although there are groups within the military who oppose the elections, we do not believe the military will renege. [REDACTED]

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To halt the economic slide triggered by the mid-1982 Falklands war, Buenos Aires backed away from populist economic policies in favor of an IMF program. The policy spurred a modest recovery, but inflation, now about 275 percent yearly for wholesale prices, has not been brought under control. Earlier this month, the economic team took steps to relieve inflationary pressures—primarily by implementing tighter controls on wages, prices, and interest rates. Soon after, however, under pressure from labor, the regime made wage and other concessions to avert a threatened general strike. Sharp public sector wage increases this year will play a major role in the collapse of the IMF program, which we expect to see by yearend. Thus, the new civilian president will be challenged to balance the demands of an aggressive labor movement with those of the IMF and international bankers. [REDACTED]

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The electoral contest will pit the traditionally predominant Peronists against the Radical Civic Union (UCR), the perennial second place finishers. Raul Alfonsin captured the UCR's nomination and is trying to broaden his party's traditional middle class appeal with a populist program aimed at attracting working class support away from the Peronists. The Peronists, with moderate Italo Luder as standardbearer, entered the contest as clear favorites and remain so, albeit with a diminishing margin. Alfonsin has an outside chance of winning because the Peronists may be unable to overcome internal divisions or project the dynamism that has characterized Alfonsin's campaign to date. [REDACTED]

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Recent well publicized sea and air incursions into the British exclusion zone around the Falklands were aimed at refocusing international attention on the territorial dispute in anticipation of UN debates. The Argentines are especially anxious to thwart London's plans to build an airbase on the islands. The draft resolution offered at the UN is moderate and should gain majority support in the General Assembly, if pre-election developments in Argentina do not alienate some backers. On the Argentine-Chilean front, despite the Pope's ongoing efforts to find a solution to the Beagle Channel dispute, negotiations are likely to remain in limbo. [REDACTED]

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[REDACTED]

Brazil

Key Domestic Issues

- o President Figueiredo's administration appears increasingly adrift, and Figueiredo himself is widely viewed as aloof and ineffective in contrast to his earlier popularity.
- o IMF-mandated austerity measures have sparked labor unrest, and economic dissatisfaction also is growing within the middle class, the business community, and the middle echelons of the armed forces.
- o Brazil's international payments position has become precarious because the IMF and foreign banks have suspended further lending pending acceptable new measures. This situation has prompted major political and business groups—as well as a majority of federal deputies—to call for a debt moratorium. [REDACTED]

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Comment

Brazil's dilemma is how to keep moving toward a return to civilian rule in 1985 while coping with an unprecedented economic crisis. Since economic recovery is unlikely within the next two years—real wages probably will continue to decline and unemployment will expand—political pressures are certain to increase. A growing political backlash could force Brasilia to withdraw pledged spending cuts and a reduction in wage indexation. In addition, continued IMF delays or refusal to endorse Brazil's revised stabilization program could provoke a government decision to declare a debt moratorium within the next several months. [REDACTED]

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In our view, the economic problems will reduce the administration's credibility but probably will not destabilize the government. Figueiredo is unlikely to regain public confidence during the remainder of his term, and he faces strong challenges from dissidents within his own party not only to austerity policies but also to his overall leadership. Nonetheless, we believe plans remain on track for a peaceful transfer of power in March 1985 to Figueiredo's successor who almost certainly will be from the ruling party. [REDACTED]

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The transition would be threatened only in the event of protracted economic decline coupled with a sharp deterioration of public order, and possibly the emergence of a charismatic politician unacceptable to the military. Such extreme circumstances would be necessary to push the high command into intervention, which we believe is a remote possibility over the near term. [REDACTED]

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[REDACTED]

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ChileKey Domestic Issues

- o A two-year economic recession and President Pinochet's refusal to accelerate the timetable for returning the country to civilian rule before 1989 have fueled the growth of a strong opposition movement this year.
- o Political and labor coalitions composed of activists from across the political spectrum have sponsored "days of national protest" each month since May and two national strikes.
- o The protests have led moderates inside the government to press Pinochet to grant concessions; the state of emergency has been lifted, and Pinochet is considering a suggestion to hold a plebiscite on amending the 1980 constitution to allow election of a congress before 1989.
- o The armed forces still support Pinochet but favor the political concessions. [redacted]

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Comment

Pinochet's non-confrontational speech on 11 September marking the tenth anniversary of the ouster of the Allende regime and the moderate level of violence during the fifth day of protest on 8 September should permit the continuation of talks begun in mid-August between the government and the democratic opposition on political liberalization. In his speech, Pinochet defended the timetable outlined in the 1980 constitution that would lead up to the restoration of civilian rule in 1989, and confirmed the possibility of an amendment that would allow the earlier election of a congress. He also took note of the dialogue between Interior Minister Jarpa and the opposition Democratic Alliance and urged them to continue discussions. [redacted]

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Pinochet's hard-line critics are unlikely to be satisfied with these concessions, however, since they are demanding his immediate resignation. Communist plans for continued violence could delay or disrupt the resumption of talks on democratic reforms. [redacted]

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Chile's economy has been in a severe recession since mid-1981. Falling prices for copper—Chile's principal export—high international interest rates, a sharp cutback in foreign lending, and severe import competition contributed to a 14-percent drop in real GDP, widespread bankruptcies, and over 20 percent unemployment in 1982. Despite government employment programs, domestic financial reforms, and IMF and external debt rescheduling agreements, Chile's economy remains troubled. A modest recovery is underway but will depend on continuing improvement in the world economy, rising demand and prices for copper, and renewed domestic financial stability. [redacted]

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Most observers believe that Pinochet will remain president as long as he maintains the confidence of the armed forces. [redacted] the armed forces still support Pinochet's continuation in office. Nevertheless most senior officers, especially in the Air Force and Navy, favor an acceleration of the transition to civilian rule. Some

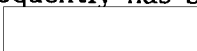
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Chile - continued -

military leaders believe that violent repression of demonstrators and publicity about corruption by members of the president's family hurt their professional image. Pinochet probably now recognizes this and consequently has been willing to make some limited political gestures toward his opponents. 

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Egypt


Key Domestic Issues

- o Egypt is moving toward a foreign financial crisis. The government is having difficulty making interest payments to the United States on FMS loans, and we believe the situation will deteriorate in the months ahead.
- o Egyptian officials discussed a standby agreement with the IMF in August, but little progress was made. 

- o President Mubarak has stayed ahead of his fragmented opposition, but domestic politics are warming up in anticipation of parliamentary elections next spring. A foreign debt crisis could give his opposition the issue it so far has lacked. 

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Comment


Egypt hopes to avoid the adverse domestic political repercussions that would accompany economic austerity measures. The government fears a repeat of the January 1977 riots over increased bread prices and wants to avoid the appearance of having economic and welfare policies dictated by the IMF and foreign donors. 

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Washington faces a blitz of senior Egyptian visitors in the coming weeks who, because of Egypt's financial difficulties, will be focusing on the aid relationship. In addition to Egypt's representatives at the IMF/IBRD annual meeting, Deputy Prime Minister and Defense Minister Abu Ghazala and Presidential Assistant al-Baz will be in Washington next week and President Mubarak will arrive after addressing the UN at the end of the month. During these discussions Egypt will seek:

- o Relief from existing interest payments on FMS loans.
- o More FMS funding to accelerate arms purchases.
- o A greater share of FMS funding as grants rather than loans.
- o Economic aid on a cash transfer basis like that received by Israel. 

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Egyptian officials will cite a host of reasons to justify increased aid. Presidential Advisor al-Baz recently told a US Embassy official that he is particularly concerned about the adverse domestic impact of austerity measures at a time when Egypt is struggling to pay interest on US loans. The public, according to al-Baz, will attribute the higher prices to US pressure to repay its loans. The Egyptians also will argue for the aid parity with Israel that they allege was promised to President Sadat. On the military front, the Egyptians will cite the need to replace aging Soviet military hardware, will raise concerns over the large Libyan arsenal, and will complain about the high cost of US equipment. 

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Outside the economic sphere, we see no immediate danger signals for Mubarak's continued rule. Although not overly popular, Mubarak has generally gained respect over



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[REDACTED]

Egypt - continued -

the past year. The government's handling of the Lebanon situation, the refurbishing of Egypt's nonaligned credentials, and improved relations with other Arab states have been well received by the Egyptian public. The opposition is poorly organized, lacks effective leadership, and has found no single issue to rally popular support. Radical elements on the left and right have been contained by security forces. Most important, Egypt's military appears supportive of Mubarak and his policies despite some grumbling over economic hardships. [REDACTED]

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Next year's parliamentary elections likely will focus increased public attention on Mubarak's policies. The opposition press already is calling for the end of martial law imposed following Sadat's assassination. The opposition parties will attempt to underscore government mismanagement of the economy and corruption. Tough austerity measures, should they be imposed, and foreign debt problems will provide the opposition with more potent issues to use against the government. Mubarak's ruling party, however, will not be seriously challenged. [REDACTED]

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IndiaKey Domestic Issues

- o According to the Indian press, public dissatisfaction is increasing with Prime Minister Gandhi's handling of continuing regional dissidence and communal conflict, particularly in Punjab State.
- o The ruling Congress Party suffered defeat in two important state elections earlier this year, reportedly because it lost the support of groups whose votes were key to past electoral victories.
- o Satisfactory weather and the end of a major labor dispute will permit a 4-5 percent rate of overall economic growth this year.
- o Inflation of about 11 percent—higher for basic consumer goods such as rice and tea—is moderately severe by Indian standards. [redacted]

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Comment

In our judgment the erosion of the Congress Party's electoral base and the rising regional and communal strife do not threaten the stability of the Indian political system in the short term. Nonetheless, we believe these developments have cumulatively eroded important elements of its future stability. Regional and communal disturbances have strained the capabilities of India's security forces, damaged the Prime Minister's image, and highlighted long-term problems resulting from her policies. The recent marked deterioration of internal security reflects in part social strains brought on by slow economic gains, but was not triggered by economic troubles. The growing trend toward centralized crisis management and party control by New Delhi has weakened state governments, which in turn have been unable to perform effectively or to stem party factionalism. [redacted]

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Press reporting and state electoral defeats earlier this year suggest Gandhi's popularity has slipped, but we believe her dominance of the Indian political scene is secure in the absence of another nationally recognized leader. Even so, the deterioration of the Congress Party's electoral base and organization is likely to reduce the Party's parliamentary majority in the next national elections. In anticipation of these elections which must be called by January 1985, two coalitions of non-Communist opposition parties have emerged with a view to mounting united challenges to the ruling Congress Party. We expect both groups—one leftist, one rightist—to have difficulty maintaining unity. In the unlikely event that either coalition should win a plurality or majority of the vote, we believe it would split over domestic policy differences. [redacted]

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At present, India's international finances are in good shape because concessional aid and IMF support sustain reserves while increased domestic petroleum production moderates the need for fuel imports. IMF-mandated policies are not a major domestic issue because they neither curb private consumption nor employment. Business reaction to the required liberalization of economic controls and restraint on the government's domestic borrowing is mixed and therefore is not a major constraint on government policy. Elite groups see the plight of Mexico and Brazil as a warning of the danger of accepting US advice to increase foreign commercial borrowing rather than seek additional funds from multilateral institutions. [redacted]

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[REDACTED]

India - continued -

In our view, there is a slightly better than even chance that within three years international financial strains will force policy changes such as greater import austerity or renewed tight controls on business activity that could arouse substantial resentment in New Delhi. [REDACTED]

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[REDACTED]

Mexico

Key Domestic Issues

- o Labor continues to support the government but has made it clear that support is not unconditional.
- o Reaction to austerity has been reflected in minor setbacks to the ruling party in local elections.
- o Generally unconnected with national policies, sporadic regional violence that is typical of the Mexican political scene continues.
- o Political tensions have eased somewhat as a consequence of the president's political skills and improvements in Mexico's external accounts. [REDACTED]

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Comment

Since assuming office on 1 December 1982, President Miguel de la Madrid has skillfully and decisively moved against the enormous political and economic problems inherited from his predecessor. His firm commitment to austerity has yielded progress toward balancing Mexico's foreign accounts and marginally slowing runaway inflation. At the same time, his tough policies have generally been regarded as fair and have not provoked unmanageable splits in the cabinet or the ruling party. [REDACTED]

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The president's solid but undramatic State of the Union Address on 1 September reassured Mexicans that the crisis will ease under the government's strong leadership. Nevertheless, holding to the program for the balance of the year will be more difficult, as it requires further deep government spending cuts, a substantial reduction in the public sector payroll, and a probable continuing decline in private business activity. [REDACTED]

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Determination and skillful negotiating tactics have gained the president the support of organized labor and earned him the grudging cooperation of business and the middle class. The unions' primary goal has been to maintain jobs for members, and so far most employment cutbacks have occurred among less skilled, unorganized labor. Tranquility on the labor front nevertheless remains conditioned on the government's ability to control prices. Private business has been pleased with wage restraints and the president's low-key, down-to-business style. [REDACTED]

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De la Madrid's improving image as a leader reflects his growing ease in office and his increasing acceptance of advice from well-chosen political and technical advisers. The president has delivered important speeches, initiated extensive legislative and administrative reforms, and played a crucial role in shaping the Contadora group's Central American initiatives. Indictment of a high-ranking member of the previous administration on charges of corruption is helping dispel skepticism about de la Madrid's commitment to curb abuses of power. [REDACTED]

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Adverse public reaction to austerity and past political abuses has been reflected in municipal election results in several important northern towns, and we expect further scattered electoral setbacks will greet the government later this year. While

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[REDACTED]

Mexico - continued -

embarrassing, these opposition victories will be no threat to the political control of Mexico's ruling party. [REDACTED]

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Sporadic regional violence, typical of the Mexican political horizon, has broken out in several places, and further isolated incidents are probable. Problems generally involve regional issues and personalities and do not represent reaction to national policies. Additional incidents are likely in Oaxaca as municipal elections approach in November. Serious unrest such as rioting in squatter settlements outside major cities has not occurred, but the de la Madrid government is quietly preparing for such contingencies and would have little trouble controlling scattered incidents. [REDACTED]

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[REDACTED]

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MoroccoKey Domestic Issues

- o A heavy foreign debt equivalent to two-thirds of the gross domestic product has significantly reduced the nation's creditworthiness; foreign exchange reserves are able to cover less than a week of imports.
- o Debt service costs that have grown to 45 percent of foreign exchange earnings and chronic current account deficits have forced Rabat to stiffen austerity measures to secure a new \$315 million IMF standby loan and to seek a debt rescheduling.
- o Deteriorating social services and declining living standards are causing discontent primarily in urban areas.
- o Popular outbursts are more likely as austerity continues, and King Hassan may have to use his security forces to quell disturbances.

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Comment

We believe that the moderate, pro-Western government of King Hassan II is secure over the short term. Islamic fundamentalists and socialists, though, remain at odds with the regime. Deteriorating economic conditions are causing increased unemployment; we are particularly concerned about the growing number of university graduates who lack avenues into the governmental patronage system. Although it is difficult to determine the impact of the worsening economy on the average Moroccan, criticism of the regime's economic policies is growing among organized labor, students, and the unemployed, and new urban unrest could result if living conditions deteriorate further. We believe that renewed economic growth and an improvement in social services and living standards are unlikely in the next several years as austerity measures are pursued. The danger is that in the interim the economically disgruntled will join with the politically and religiously disaffected and threaten the regime.

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Depressed phosphate earnings and the need once again to increase food imports because of drought have aggravated the government's financial difficulties and compelled Rabat to seek new external assistance in addition to a recently negotiated \$315 million IMF standby loan. The government's ability to obtain additional loans from abroad will remain in doubt until Morocco's debt rescheduling is completed. Saudi aid probably will be resumed because of Morocco's belt tightening efforts but is likely to remain below previous levels because of Riyadh's decreased oil revenues. Financial pressures could necessitate a sharp cut in non-food imports. If the King fails to obtain foreign assistance or if military deliveries are delayed as a result of the government's not meeting repayment obligations, which it is having difficulty doing, the regime could become the focus of opposition rhetoric and of anger within the military.

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The King's reluctance to entertain criticism and advice on the economy, together with his preoccupation with foreign policy, is increasing his isolation as well as the risk that remedial economic measures will not be consistently pursued. Although the government has stiffened austerity measures to deal with its growing economic problems, Hassan has been reluctant to follow IMF recommendations, particularly a reduction of food subsidies. A cut in food subsidies in June 1981 sparked bloody riots in Casablanca in

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Morocco - continued -

which 100 people died. We expect that the security forces, which strongly support the King, would be able to restore order in the event of new turmoil, but only after some violence. [redacted]

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Communal elections in June passed with little disturbance but occasioned an uproar of allegations of regime interference. Parliamentary elections now scheduled for 1984 may prove more heated and could produce more serious confrontations between security forces and voters. The economy probably will be a major political issue in these elections. [redacted]

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We do not expect that the government will be compelled by its current economic problems to alter its Western Sahara strategy in the near term. If Rabat were to sharply reduce defense spending for the campaign, however, we believe military morale would be badly shaken. The military also would be disturbed by a political settlement of the dispute that, in their view, conceded too much to the insurgents. [redacted]

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Nigeria

Key Domestic Issues


- o Opposition claims that last August's national elections were rigged in favor of the governing National Party will likely promote a greater level of political controversy over the next four years than characterized President Shagari's first term.
- o Prolonged austerity could heighten ethnic tensions, especially in the more economically developed and largely opposition controlled Yoruba and Ibo states. They could claim that they are being made to bear the brunt of economic retrenchment.
- o Shagari's commitment to genuine austerity and economic reform could be undermined by pressures within his own party for patronage rewards and for scrapping or modifying what are perceived to be externally imposed economic policies.
- o Widespread economic protests could erode public support for still fragile civilian institutions and serve as a justification for a military coup. 

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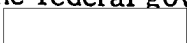
Comment

In our judgment, Nigeria's persistent economic difficulties coupled with continuing controversy over the extent of Shagari's sweep of last August's national elections will tax the president's considerable political skills as he begins his second term. Shagari has proven adept in the past at juggling diverse political, ethnic, and economic interests while maintaining his image as a strong and impartial national leader. We believe his public support could begin to wane, however, if he fails to act on his campaign promises to make extensive cabinet changes, curb corruption, create new states, and get Nigeria's economy moving again. Moreover, now that he enjoys a comfortable legislative majority, he no longer can blame Nigeria's economic and political difficulties on opposition obstructionism. 

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Little economically inspired protest has been reported thus far, but we believe prolonged austerity—if it is perceived as not being applied equitably—could heighten ethnic tensions, the root cause of most political instability in Nigeria. In particular, we believe Shagari is vulnerable in urban areas in Yoruba and Ibo dominated states. Many of these states are still controlled by opposition governors who we expect will attempt to capitalize on economic hard times by blaming the federal government for their troubles. 

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We do not believe there is,  extensive support within the military for a coup at this time. Widespread protests over food shortages or worsening economic conditions, however, could serve as a pretext for an attempted coup as could persistent political bickering that diverts the federal government from tackling the country's pressing economic and social problems. 

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PakistanKey Domestic Issues

- o President Zia ul-Haq announced plans on 12 August to restore the constitution, end martial law, and reinstate civilian government by March 1985. The military apparently supports his measures.
- o The left-center, eight-party Movement for the Restoration of Democracy has rejected Zia's program and begun a civil disobedience campaign to force him from office. Conservative and religious politicians are also critical but so far have disavowed the campaign.
- o The anti-Zia campaign has accomplished little outside Sind Province and would have to spread to Punjab before it would threaten Zia's rule. Widespread disturbances in Sind reflect regional discontent with the political and economic policies of the Punjabi-dominated government.
- o Students and labor have largely ignored the agitation, but student organizations may begin protests if Zia carries through plans to ban college student unions.
- o National economic issues have not been a significant factor contributing to the unrest in Sind. The relative prosperity of the country has made it difficult for the anti-government forces to carry the demonstrations to other parts of the country. Even so, social and economic discrimination against Sinds is a key issue in the current unrest. [redacted]

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Comment

President Zia ul-Haq is coping successfully with the current disturbances in Pakistan, the most serious threat to his rule so far. We believe his regime's capable handling of serious anti-government rioting in Sind Province and the unwillingness of Pakistanis in other provinces to join the protest movement increase the chances that Zia and the army will continue to guide Pakistan's political future for at least the next one to two years.

- o Zia's authoritarian regime has avoided overly repressive policies, although it has dealt firmly with organized demonstrations. It has given the country more than six years of domestic stability and substantial economic progress.
- o Zia also has dealt effectively with external threats. He has stood up to the Soviets on Afghanistan and has improved relations with India. He has succeeded in gaining major economic aid and arms assistance from the United States. [redacted]

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The president ultimately depends on the Army to remain in power. We believe most senior officers support Zia's plan for a phased return to civilian government and a permanent oversight role for the armed forces. No ruler, however, can be certain of the

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[REDACTED]

Pakistan - continued -

army's support if it is called upon to put down civil disorders, particularly in the all-important province of Punjab. [REDACTED]

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Zia's main opposition, the Movement for the Restoration of Democracy (MRD), is poorly organized and lacks both a popular issue or an effective leader to galvanize a nationwide anti-Zia campaign. [REDACTED] the protest movement in Sind Province this summer was launched largely by the Pakistan People's Party of former Prime Minister Bhutto. The PPP has substantial support among the urban and rural poor of Punjab but has found it difficult to mobilize this support in the absence of a strong leader. [REDACTED]

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President Zia has promised to hold provincial and national elections by March 1985, amend the constitution to create a strong presidential system, and withdraw martial law. His statements suggest he will bar hostile opposition parties, including the PPP, from participating in the elections. [REDACTED]

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Given the right circumstances, we believe a nationwide opposition movement could arise rapidly and with little warning. In such an event, the army probably would replace Zia with another general who would negotiate a return to civilian rule on terms the army could accept. In our view, the army would attempt to preserve the present US-Pakistan relationship, but if a Pakistan People's Party government succeeded in taking over, US-Pakistan ties, as well as Pakistan's stand on Afghanistan, probably would be significantly weakened. [REDACTED]

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While the reasonably strong economy is currently a bright spot that Zia can exploit for political purposes, he will be looking for any danger signals. These include any serious downturn in the economy that impacts on the cost and availability of essential commodities and services and encourages urban demonstrations against the government, and any rapid return of workers from the financially-pressed Gulf state that would lead to foreign exchange shortages and greater unemployment at home. [REDACTED]

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[REDACTED]

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Peru

Key Domestic Issues

- o Buffeted by internal security, political, and economic difficulties and by natural calamities, the Belaunde administration, we believe, is losing popularity and credibility.
- o The Sendero Luminoso (SL) insurgent group's expanded operations in rural Ayacucho and in Lima have heightened public anxiety and not helped relations between the president and the military, which wants more unrestricted counterinsurgency authority.
- o Unparalleled climatic disasters have aggravated the recession, caused food shortages, contributed to inflation, and curbed needed export earnings.
- o Growing factionalism in the governing party and the resurgence of the major opposition party are weakening Belaunde's political base; we believe he may face setbacks in the November municipal elections.

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Comment

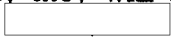
We do not believe that the insurgent threat or economic pressures will result in a coup or other major upheaval during the next six months. Also, in our view, the SL's limited popular appeal and lack of foreign support severely limit its prospects. At the same time we believe that the insurgents' political-military apparatus is largely intact despite their recent heavy casualties. We share the Peruvian military's assessment that eliminating the SL could take two to three years and prove costly.

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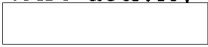
Public support for decisive action against the SL is widespread, and we believe Belaunde will soon order the military to take total control of counterinsurgency operations. The security forces' effectiveness, though, will continue to suffer from deficiencies in equipment, training, intelligence capabilities, and tactics. We are concerned that if the security forces employ more brutal methods, they will alienate local communities and thereby further delay progress against the SL.

25X1



Peru's economy is suffering a severe setback owing to natural disasters, depressed commodity prices, and IMF-mandated austerity programs. Unemployment and food prices are rising and imports declined by \$1 billion in 1982. Bankers have pulled together a financial rescue package, but Lima's foreign financial position will remain precarious until exports rebound. Economic contraction and high inflation are sparking protests against austerity and putting pressure on Belaunde to loosen tough economic policies, a move that could cause difficulties with the IMF and foreign creditors. The government reportedly intends to ask the IMF to ease some restrictions on the standby credit, especially the requirement that the deficit be held to 4.1 percent of GDP. Although global recovery would make these problems more manageable, grim economic conditions and increased terrorist activity may undermine investment and force foreign firms to curtail operations.

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[REDACTED]

Peru - continued -

Belaunde's position will be tenuous, but his greatest asset is the absence of any alternative; both the military and the opposition are reluctant and ill-prepared to assume power. The armed forces desire to confine themselves to professional military pursuits and lack the inclination or confidence to tackle Peru's intractable socio-economic ills. The leftist coalition is divided and losing popularity. Moderate parties will increase pressure on Belaunde, but they fear military intervention and the destruction of their own political future if civilian government is totally discredited. [REDACTED]

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[REDACTED]

25X1

PhilippinesKey Domestic Issues

- o Moderate opposition participation in the 1984 National Assembly elections, a possible watershed in the liberalization of post-martial law politics, is in doubt as the opposition renews threats to boycott the elections in the wake of the Aquino assassination.
- o Manila is concerned that the assassination of Aquino will cause President Reagan to reconsider his planned visit to the Philippines in November.
- o Manila also fears that Congress will alter the terms of the recently approved \$900 million military base assistance package as a result of unhappiness with Marcos's human rights policies.
- o The Philippines' external financial situation has become increasingly precarious in recent months, and Manila has begun sounding out Washington for emergency financial assistance. [redacted]

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Comment

Manila has weathered the initial storm over Benigno Aquino's assassination, and we believe its prospects for continuing to do so over the next few months are reasonably good. Aquino's death, however, will leave the domestic political environment, the country's external finances, and Philippine foreign relations unsettled for some time. [redacted] the majority of the political opposition— and possibly the majority of the population— believe that the government was involved in the assassination. [redacted]

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We believe the government is pressing its investigation of the murder with some vigor, but it has handled public relations poorly. An independent commission of inquiry was established, but it has had great difficulty filling its membership with credible public figures. Filipinos appear to expect little from the investigation; the popular views of the commission's potential for independent inquiry are polarized along the lines of existing political loyalties. [redacted]

25X1

Aquino's death has overshadowed several other recent developments bearing on domestic stability. Succession jockeying appears to have intensified as a result of the health problems Marcos experienced in August. Several close associates of the President apparently assumed the worst about his condition and moved to align themselves with Imelda Marcos. Despite constitutional provisions that the Executive Committee serve as an interim government, many politicians inside the ruling party assume that Imelda Marcos will take the reins of power in the event that Marcos becomes incapacitated. [redacted]

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Serious infighting had already surfaced in the defense establishment, and it appears one result is that the military's potential role in the post-Marcos era may be significantly increased. Longstanding tensions between Defense Minister Enrile and Armed Forces Chief of Staff General Ver broke out into open conflict in late July when, [redacted] President Marcos summoned Enrile into his office to

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[REDACTED]

Philippines - continued -

question his loyalty and to inform him of an impending reorganization of the defense establishment. Since Ver became Chief of Staff, he has consolidated control of the military by placing officers loyal to him in key military units and in headquarters staff positions. [REDACTED]

25X1

The Philippines' external finances have become increasingly precarious in recent months with Central Bank liquidity severely strained; its short-term debt of \$2.5 billion requires immediate attention to avoid a foreign exchange crisis. Manila has implemented new financial austerity measures in an effort to cope, and domestic political reaction to them has so far been minimal. Fourth quarter 1983 government spending will be sharply cut back, and the 1984 government budget plans a 34-percent reduction in capital outlays. Nonetheless, Manila's 8-percent devaluation of the peso in June appears to have been too modest to ease pressures on Central Bank foreign exchange reserves. [REDACTED]

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Marcos is aware that international attention will be focused on President Reagan's visit in November. He had expected it to enhance his international status as a statesman and put the stamp of legitimacy on his government at home. Marcos now almost certainly fears that events connected to Aquino's death may force the cancellation of the visit. [REDACTED] many US banks would interpret a cancellation as a sign that Washington lacked confidence in the Marcos government, leading them to withdraw credit lines. [REDACTED]

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After several months of debate within the ruling party, Marcos has yet to decide on election rules and party accreditation. His challenge is to find a way to simultaneously ensure a victory by the ruling party, induce participation by the moderate opposition so as to legitimize a ruling party victory, and appear fair in setting the rules of the game. Since the assassination, the moderate opposition appears as disorganized as ever and without a replacement for the charismatic Aquino. Should they decide to boycott the election, it would cost Marcos the legitimizing factor he so dearly wants, but it would also ensure the moderate opposition irrelevance in the country's political future. [REDACTED]

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[REDACTED]
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Saudi Arabia

Key Domestic Issues

- o The drop in Saudi oil revenue triggered by a decline in international demand for oil is confronting Riyadh with its most difficult financial problems since the oil boom began in 1973.
- o To cope with lower revenues, the government is curbing domestic spending, drawing from its large foreign reserves, and curtailing some of its foreign aid disbursements.
- o Cuts in government outlays are inflicting financial hardships on the business community, but criticism remains low-key and as yet poses no serious political problems for the regime.

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Comment

The fall in revenue is having a profound psychological impact on the regime. Whereas many ministries in the past few years had a surfeit of funds, they must now compete even for routine allocations.

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The government is taking a broad approach to ease financial dislocations. In addition to drawing down foreign assets, the regime is delaying payments to government contractors—especially expatriate firms—and imposing a moratorium on new government contracts. Work on non-essential development projects has halted, and new investment for some oil facilities and other projects is being cut back. The government also is showing reluctance to maintain existing levels of foreign aid to several traditional recipients, including Somalia and Morocco.

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25X6



Fahd is being careful to avoid austerity measures that could provoke political unrest. He apparently has ruled out cuts in key government subsidies and social programs that would hurt middle and lower income groups. Saudi businessmen hurt by the slowdown in contract payments are unhappy, but the King has helped dissipate criticism by ordering foreign firms to subcontract a larger share of their business to Saudi companies.

25X1



25X1