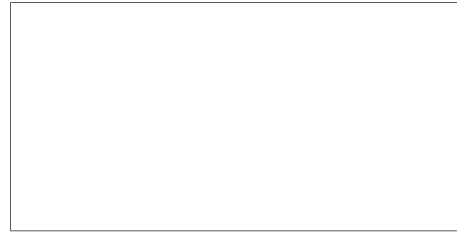




**Director of
Central
Intelligence**

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OCPAS/CIG



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*Saturday
13 August 1983*

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WEST GERMANY: Reactions to "Dual-Key" Proposal

Bonn is unlikely to raise the issue of dual control for US INF missiles, despite recent media attention to an interview by Christian Social Union leader Strauss advocating such a system. [Redacted]

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Following press reports of Strauss's statement, a Defense Ministry spokesman has emphasized that no such proposal is being considered. Chancellor Kohl has rejected suggestions of a West German right to veto the use of US nuclear missiles. The US Embassy in Bonn reports that Strauss's remarks came in response to a leading question by the interviewer and is not a trial balloon by the governing coalition. [Redacted]

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[Redacted]

Comment: The Kohl government regards existing consultation arrangements with the US as entirely adequate and would prefer to avoid a political debate on the sensitive topic. While some opposition leaders may attempt to exploit the interview to embarrass the government, the Social Democrats would find it difficult to endorse proposals for dual control of INF. Most prominent political leaders in West Germany, including Social Democratic Party leader Vogel, have opposed any arrangements that would appear to give Bonn even partial control over nuclear weapons. [Redacted]

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USSR-EASTERN EUROPE: Andropov's Position on Economics

A Soviet diplomat in Eastern Europe reports that General Secretary Andropov has expressed concern about some Polish and Hungarian reform proposals. [Redacted]

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The diplomat reports that Andropov was displeased with a proposal by some Polish leaders to expand their private economic sector. He also expressed misgivings over proposals to expand factory autonomy made by Hungarian leader Kadar during his recent visit to Moscow. The diplomat claims that the Hungarians had approached the limits of what is permissible on economic reform and that Moscow is increasingly concerned with Budapest's Western economic orientation. [Redacted]

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The Soviet official insists, however, that Andropov recognizes the need to permit differences among "socialist" states and claims that the Soviet leader favored evolutionary change to revitalize "socialism." The US Embassy in Budapest says that the Hungarians remain confident that Andropov still supports the main thrust of their reform program. [Redacted]

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Comment: Some of Andropov's colleagues may be urging him to restrain East European reform moves. The diplomat's comments, however, do not suggest that Moscow intends to reverse existing reforms. [Redacted]

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The Soviets have been critical of the role of the private sector in Poland, and Andropov is likely to resist greater concessions to it by Warsaw. He has been a strong supporter of Hungarian economic reform, but he may now feel that managerial autonomy there has gone as far as it can without undermining the "socialist" system. [Redacted]

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Budapest appears committed to further price and wage reform, the breakup of large enterprises, and increased economic ties to the West. It sees these as essential to solving the country's economic problems. Kadar may, however, back off from more far-reaching proposals to satisfy his critics in Moscow. [Redacted]

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Andropov's reported views suggest he realizes that East European experience will provide no quick fixes and that he will be wary of relying on market mechanisms to revitalize the Soviet economy. [Redacted]

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EL SALVADOR: Arms Interdiction Effort

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The Salvadoran Army intercepted a large insurgent supply column in San Vicente Department earlier this month and captured several prisoners. It believes the 300-man guerrilla force was en route from supply depots in southeastern Usulután Department to its stronghold on the Guazapa Volcano. [Redacted]

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[Redacted]

Comment: Large shipments of arms and munitions apparently are continuing to reach the southeast for subsequent distribution overland to the various guerrilla fronts. The operation also verifies the insurgents' continued dependence on external sources for weapons and supplies, despite their past successes in capturing materiel from the armed forces. [Redacted]

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ARGENTINA-UK: Incidents in South Atlantic

Several recent incidents initiated by Argentina near the Falklands are designed to focus international attention on the issue again, in anticipation of new debates at the UN. The Argentine Navy reportedly has encouraged fishing vessels to sail into the British protection zone surrounding the islands, [Redacted]

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[Redacted] London has publicly warned Buenos Aires of the possibility of military retaliation. [Redacted]

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Comment: Argentina also is trying to build support—especially in the US Government—to stop British plans to construct an airbase on the islands and to persuade the UK to open rich fishing beds in the protection zone to Argentine ships. London probably will not retaliate unless the incursions become more serious. The British warning is intended to portray Buenos Aires as an aggressor and to help justify the decision to build the base. [Redacted]

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CHILE: Crackdown Produces Violence

The violence following President Pinochet's decision to crack down on participants in the nationwide protests on Thursday probably will increase pressure from elements within his government to accelerate political concessions. Government spokesmen report 17 deaths, [Redacted] as troops and police used tear gas, clubs, and automatic weapons against the demonstrators. A prominent civilian conservative favoring a political opening and the return of exiles was sworn in on Wednesday to replace an Army general as Interior Minister. [Redacted]

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Comment: The demonstrations were the most extensive and violent so far, and the funerals for those killed could prompt more violence. The security forces' lack of discipline [Redacted] will offset any positive effects of the recent cabinet changes. Pinochet faces increasing concern in the military over the lack of order and a bolder and more unified opposition. Unless significant progress is made soon toward civilian rule, a political crisis is likely to develop. [Redacted]

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NIGERIA: Gubernatorial Elections

Voters are to elect governors for Nigeria's 19 states today in the second of five weekly rounds of elections. In the elections in 1979, President Shagari's ruling National Party captured governorships in only seven states. Opposition party reaction to President Shagari's reelection last weekend has been muted, although several of the defeated candidates are protesting the results in court. [Redacted]

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Comment: The opposition is making a concerted attempt to weaken Shagari's National Party at the state level, where governors control the political process. If the opposition parties succeed in retaining a majority of the governorships, they probably will carry the National Assembly elections later this month. Such an outcome would force Shagari to negotiate an alliance with one or more of the opposition parties in order to pass legislation. [Redacted]

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WEST AFRICA-ISRAEL: Interest in Diplomatic Relations

Recent reports from US Embassies indicate that sentiment may be building among moderate West African governments to renew diplomatic ties with Israel. Although Liberia has vacillated for years, Head of State Doe plans to announce the restoration of relations soon—perhaps today—and to visit Israel later this month. Ivory Coast President Houphouet-Boigny has urged Israel to delay Liberia's move while he attempts to persuade "five or six" other unnamed African countries to follow suit. Malawi, Lesotho, Swaziland, and Zaire are the only black African countries that now maintain diplomatic ties with Israel. [Redacted]

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Comment: Reestablishing relations with black African countries—most of which severed ties after the 1973 Middle East war—has been a major objective of Israeli foreign policy. West Africa's renewed interest in relations with Israel stems in part from displeasure with Libya's latest intervention in Chad. In addition to rebuking Tripoli, the countries also seek security and economic assistance to help defend themselves against Libyan subversion.

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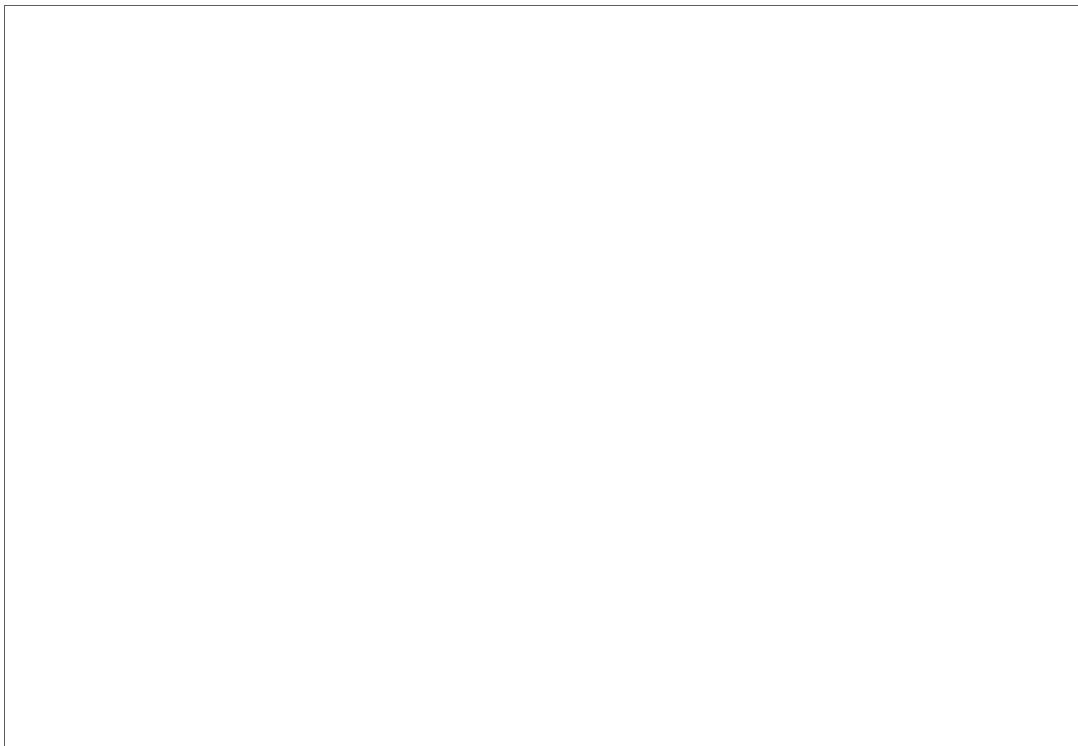
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USSR: Criticism of the Police

Pravda on Wednesday carried an article by Minister of Interior Fedorchuk berating the police for their inability to combat theft of state property. Fedorchuk also drew attention to the role of drunkenness in criminal activity, and called for stricter punishment of drunkards. In addition, he indicated a purge of the Ministry was under way. [Redacted]

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Fedorchuk won a reputation as a strict disciplinarian who was ruthless in stamping out dissidence when he headed the Ukrainian KGB and during his brief tenure last year as KGB chief. He became the Minister of Interior in December, [Redacted]

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[Redacted]

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Two weeks ago the Politburo decided to designate political officers in the Ministry to improve party control and heighten discipline.

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[Redacted]

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Special Analysis

EGYPT: Potential Financial Crisis

Looming financial difficulties could force the Egyptian Government to make politically difficult economic austerity decisions and perhaps strain relations with the US. Cairo already is having some problems servicing its foreign debts, and lower oil earnings will cause foreign exchange difficulties to become worse in the months ahead. If Egypt fails to adjust to lower oil earnings, it could be faced with a debt crisis late this year or in 1984. After several years of increases in production and income, the tightening foreign financial situation is slowing economic growth. [redacted]

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Egypt has weathered the soft oil market and the global recession better than most developing countries. Its generally good performance to date stems from a fortuitous decline in the prices of key agricultural imports and from the limited policy adjustments carried out by the government. [redacted]

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The government reduced oil prices five times in 1982 to ensure sales, and it pushed oil production to a record high of 700,000 barrels per day in the fourth quarter. It also has used direct controls to restrict imports and has tightened domestic credit ceilings. Moreover, falling world prices for food grains and sugar, which comprise nearly one-fourth of Egypt's imports, have helped compensate for reduced oil earnings. [redacted]

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Nevertheless, overall economic growth in 1982 is estimated to have slowed to around 6 percent because of the tighter foreign exchange situation. Although this was a favorable performance when compared with that of most developing countries, it was lower than the 8- to 9-percent increases of recent years. [redacted]

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Inflation rose to 13.3 percent in 1982, as compared with 10.2 percent in 1981. Price increases were encouraged by rapid monetary expansion, which in turn was caused by government deficits equivalent to 20 percent of gross domestic product. [redacted]

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Problems Increasing

The government has been especially concerned about declining world oil prices. To respond to market pressures and to try to maintain sales, it cut oil prices in each of the first three months of

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1983 by a total of \$4.50 a barrel. As the oil market became somewhat more steady in the spring, however, Egypt raised prices by 25 cents a barrel in May and again in June and 50 cents a barrel at the beginning of July. [redacted]

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Foreign exchange difficulties persisted in the first half of 1983 and will become worse in the months ahead, when the effect of lower oil earnings is felt. Barring new setbacks, the government should be able to muddle through the next few months, but financing an estimated current account deficit of \$3 billion will not be easy. [redacted]

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The most recent data indicate that Egypt had only \$750 million in foreign exchange reserves at the end of March, enough to pay for only one month of imports. Foreign aid receipts are not likely to increase much over 1982. Most US and other Western banks, although willing to maintain credit lines, are increasingly wary of providing new balance-of-payments loans to Egypt. [redacted]

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Possible Foreign Debt Crisis

Foreign bankers and the IMF will be watching Egypt's financial situation closely. Cash flow problems, similar to those that caused recent late payments to the US for credits under the Foreign Military Sales program, are likely to recur. [redacted]

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There are several other possible developments that could cause Egypt's debt problems to intensify rapidly:

- Any additional reductions in the price of oil would be costly because Egypt loses about \$125 million annually for each \$1-per-barrel decline in prices.
- Increased agricultural import prices would push up the cost of essential food imports that are used for government-subsidized food distribution programs.
- A foreign lender crisis, stemming either from Egyptian or other Third World debt problems, could reduce Cairo's ability to refinance short-term credits and would create major liquidity problems. [redacted]

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The likelihood of these events occurring is small. Any one of them, however, would be a major setback. [redacted]

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Cairo has taken several small corrective steps, but additional and more far-reaching measures almost certainly will be necessary to avoid a crisis or to cope with one after it occurs. There is no consensus, however, on what actions are necessary. The government is likely to delay reforms because of its fears about the political repercussions of austerity. [REDACTED]

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Implications of a Debt Crisis

A foreign debt crisis would have serious domestic and foreign repercussions. Past foreign financial crises are associated in Egypt with traumatic political events, such as the bread price riots of January 1977 that shook the Sadat regime. [REDACTED]

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In recent months there has been increased grumbling about rising prices, failing public services, and other economic hardships. A foreign debt crisis and the specter of foreigners dictating Egyptian economic policies would give opposition groups potent issues to use against President Mubarak. [REDACTED]

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A debt crisis also would complicate relations with the US, Egypt's largest creditor. Cairo already has tentatively explored the possibility of relief from payments due on US Foreign Military Sales credits. If Egypt could not service its debts to the US, the strict procedures used by Washington to deal with such problems would, in Cairo's view, directly contradict the special political relationship Egypt believes it has established with the US. [REDACTED]

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A debt crisis would prompt Egypt to intensify efforts to achieve aid parity with Israel. It would, for example, seek cash transfers of economic aid and greater forgiveness of military assistance loans. Mubarak and other Egyptians claim that such aid parity was promised to the late President Sadat, and the need for more generous US help would increase as Egypt's problems worsened. [REDACTED]

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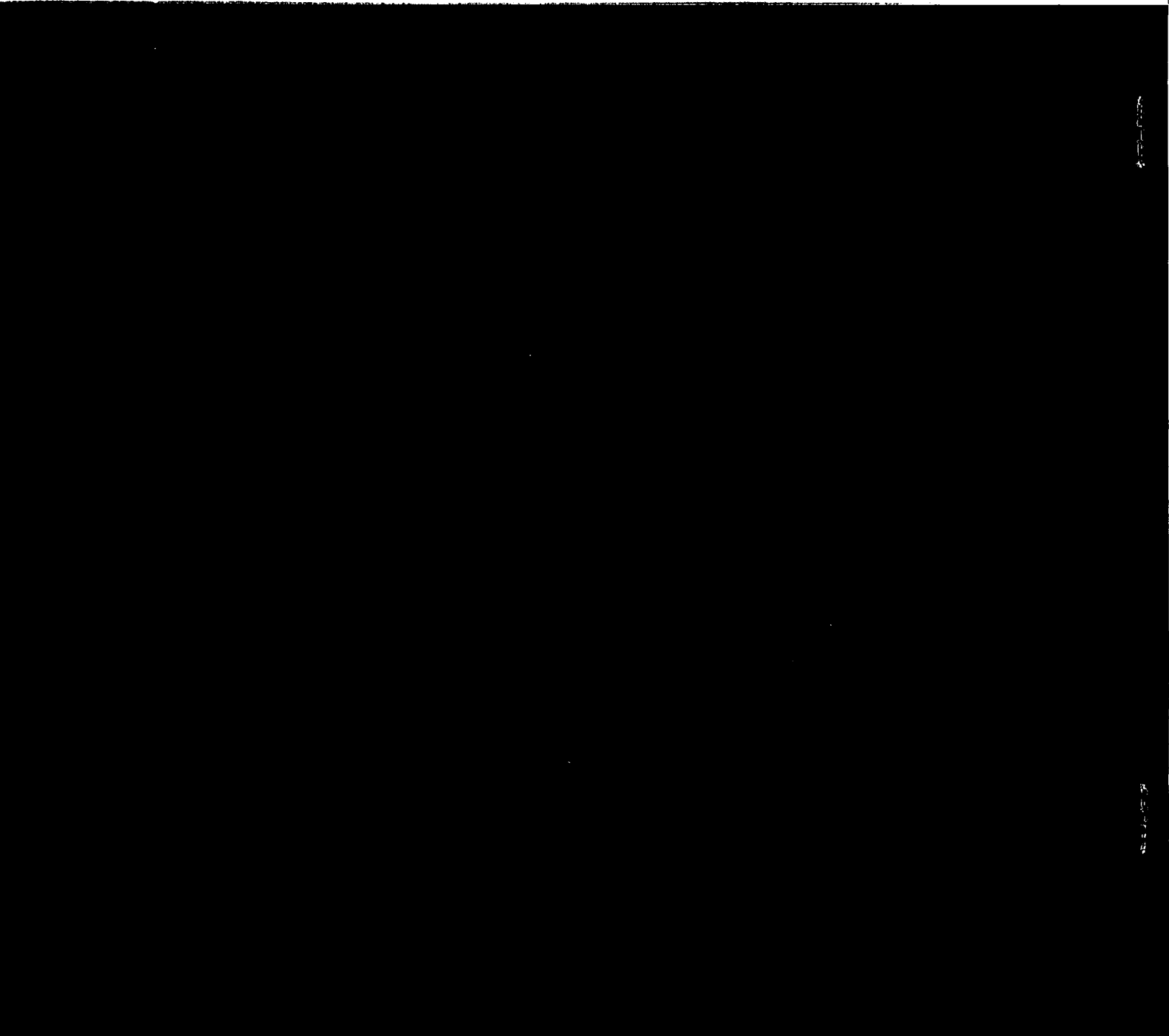
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