25X1

Directorate of
Intelligence

~~Secret~~

International
Economic & Energy
Weekly

25X1

7 February 1986

~~Secret~~

DI IEEW 86-006
7 February 1986

Copy 841

Page Denied

Declassified in Part - Sanitized Copy Approved for Release 2011/12/08 : CIA-RDP88-00798R000300020005-4

Secret
[redacted] 25X1

International Economic & Energy Weekly [redacted] 25X1

7 February 1986

[redacted] 25X1

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

25X1

Secret
DI IEEW 86-006
7 February 1986

Declassified in Part - Sanitized Copy Approved for Release 2011/12/08 : CIA-RDP88-00798R000300020005-4

 25X1

International
Economic & Energy Weekly 25X1

Synopsis

1 **Perspective—Capital Flight and Political Events** 25X1

While most of the capital flight over the past few years has been economically motivated, political uncertainty and government corruption have been major factors in the Philippines, Nigeria, and Argentina. The structural reforms necessary to stem the outflow of capital, however, are difficult to implement because the financial interests of powerful political constituencies would suffer. 25X1

3 **Nicaragua: The Growing Consumer Squeeze** 25X1

Nicaraguan consumers are tightening their belts as the economy deteriorates and the regime commits an ever larger share of its budget to the war effort. Prospects for improvement are bleak, and the regime will rely on shipments from the Soviet Bloc to maintain minimum consumption levels while using state-of-emergency powers to prevent open discontent. 25X1

7 **The USSR's Eastern Coal Basins: A Potential White Elephant** 25X1

Expanded use of coal underpins the Soviet Long-Term Energy Program despite Moscow's current focus on oil and natural gas. We believe that coal production and utilization will probably increase only slightly—if at all—during the coming decade, leading to energy constraints beginning sometime in the 1990s. 25X1

11 **LDCs: Obstacles to Foreign Investment** 25X1

Significant increases in foreign investment are blocked in many LDCs by economic and policy barriers ranging from weak markets to poor investment climates. A number of these barriers could be lowered if LDC governments would adopt some key policy reforms, but the high political costs of the policy action required will make it difficult for most developing countries to overcome these obstacles over the next few years. 25X1

17 **Stagnant Caribbean Exports: Continuing Drag on the Regional Economy** 25X1

Despite access to preferential trade arrangements, such as the Caribbean Basin Initiative (CBI), Caribbean exports continue to decline, both to the United States and other developed countries. Declining exports are hurting the region's domestic economies and their effects are exacerbating political problems. 25X1

[redacted] 25X1

International Economic & Energy Weekly [redacted] 25X1

7 February 1986

Perspective

Capital Flight and Political Events [redacted] 25X1

While most of the capital flight over the past few years has been economically motivated, political uncertainty and government corruption have been major factors in the Philippines, Nigeria, and Argentina. Even in economically sound South Africa, a slight positive inflow of capital before the most recent period of black unrest began shifted to a $2.2 billion net outflow of private capital in the following six months. Similarly, [redacted] at least $10 billion flowed out of the Arab states during 1978-79 as the revolution in Iran, the terrorist attack in Mecca, and the Soviet invasion of Afghanistan led people to question the stability of the world's key oil-exporting region. [redacted] 25X1 25X1

Capital flight frequently builds as political uncertainty develops. Elections where the outcome or the policies of the likely winner are in doubt may lead to an acceleration in capital flight in the months and weeks leading up to the balloting. In Israel, for example, against a background of economic difficulties, capital flight picked up momentum as the July 1984 elections drew near. Likewise, when a government's longevity is clearly in question, assets will move out of the country. This pattern was visible in Iran as the Khomeini forces gathered strength against the Shah. [redacted] 25X1

Capital flight can almost always be expected following unanticipated political events such as assassinations or coups. In the wake of the Aquino assassination in the Philippines, bankers estimate that capital flight reached $5 million a day, draining reserves and forcing a debt moratorium two months later. The Philippines, however, had been suffering from political and economic malaise long before the assassination. Earlier that summer, Marcos's health problems had prompted fears of a destabilizing power struggle. [redacted] 25X1 by the time of the Aquino assassination, most businessmen had already shifted the majority of their liquid assets abroad. Much of the subsequent capital flight was actually disinvestment. [redacted] 25X1

Under authoritative governments where elites face no serious monitoring from opposition parties, movement of capital by government officials, their political associates, or family members is often prevalent. The Somoza government in Nicaragua virtually drained the central bank before Somoza was ousted in 1979. Similar charges have been leveled against members of the Marcos government who have large holdings in the United States, [redacted] 25X1

When periods of prolonged political instability or uncertainty occur, people begin to follow their money out of a country. As evidence of a tremendous "brain drain" in the Philippines, lavish homes are being sold at bargain prices. [redacted] In South Africa, white emigration in July and August was up 60 percent over the same period in the previous year, according to official government figures. Similar episodes of South African emigration occurred after the Sharpsville riots in 1960, and during the two years following the Soweto shootings in 1976. [redacted] 25X1 25X1

The political hazards that capital flight leaves in its wake are acute. Successor governments inherit overwhelming debt burdens and an empty till, leading them to question the "legitimacy" of their debts. The Alfonsin government in Argentina is a case in point. Such debtors say they will not "sweat" to pay back loans made by bankers who knew the money was being spent not for economic development but to enrich corrupt officials. At the same time, commercial banks, multilateral institutions, and OECD governments are reluctant to continue to fund countries where capital flight is an ongoing problem. The structural reforms necessary to stem the outflow of capital, however, are difficult to implement because the financial interests of powerful political constituencies would suffer. [redacted] 25X1

[redacted] 25X1

Nicaragua: The Growing Consumer Squeeze [redacted] 25X1

Nicaraguan consumers are tightening their belts as the economy deteriorates and the regime commits an ever larger share of its budget to the war effort. The Sandinistas' gradual socialization of the economy has led to a highly centralized distribution system, but rationing of basic foods—which began in 1983—is increasingly haphazard. Declining real wages have eroded purchasing power—food shortages and a phaseout of subsidies have led to soaring staple prices. Prospects for improvement are bleak, and the regime will rely on shipments from the Soviet Bloc to maintain minimum consumption levels while using state-of-emergency powers to prevent open discontent. [redacted]

Food Distribution Controls

On seizing power in mid-1979, the Sandinistas centralized food distribution through the newly created National Basic Foods Corporation, which was given sole authority to import, export, and wholesale basic foodstuffs. Over time, [redacted] the organization:

- Took over the previously privately owned supermarkets in Managua.
- Created "people's stores" to supply basic goods at subsidized prices.
- Supplied foodstuffs to commissaries in some workplaces throughout the country; these commissaries were replaced in mid-1985 by two central commissaries in Managua.
- Furnished priority supplies to some private stores, in exchange for pledges to sell controlled items at official prices.
- Built marketplaces with stalls for private vendors in neighborhoods throughout Managua with the apparent hope of closing the Eastern Market, the capital's bastion of small-scale free enterprise.
- Subsidized foodstuffs and consumer goods by enforcing wholesale and retail price ceilings. [redacted]

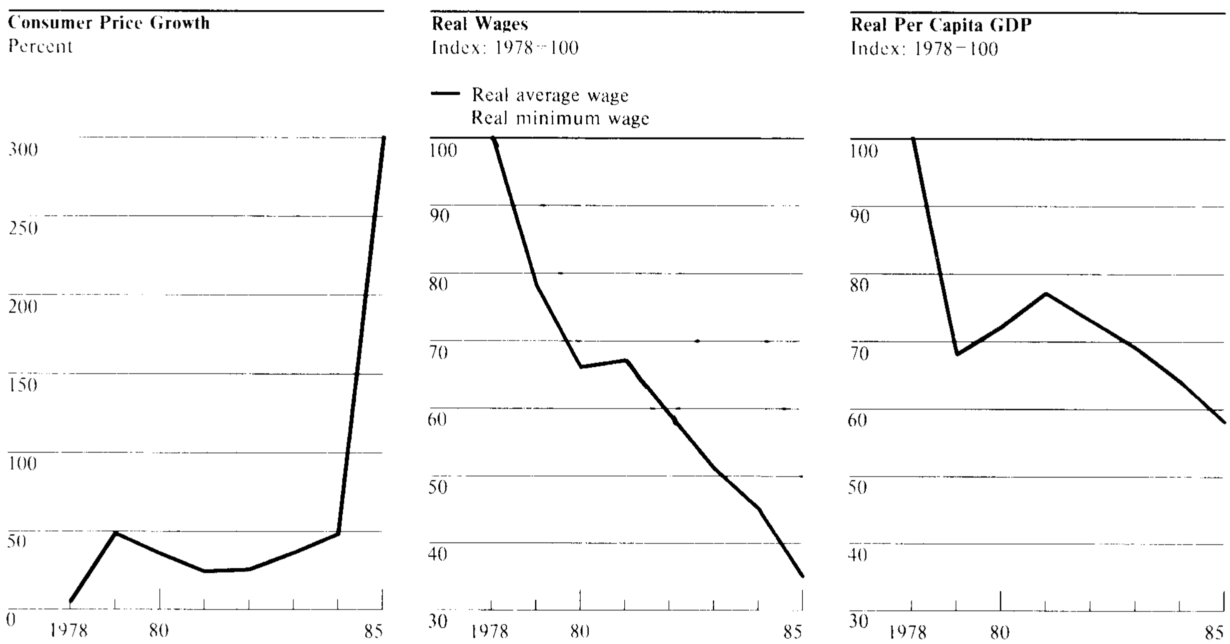
25X1

During the first two years of Sandinista rule, food imports and donations compensated for the sharp decline in agricultural production during the revolution. Per capita food imports jumped more than threefold in 1980 and remained steady the following year, according to press and US Embassy reporting. By 1982, however, a falloff in donations and the growing shortage of foreign exchange limited the flow of foodstuffs from abroad, leading to frequent shortages. [redacted] 25X1

In response, Managua set up a system of "guaranty supply cards," first for sugar, then later for rice, beans, corn, cooking oil, salt, sorghum, and soap. 25X1 Each family was guaranteed the right to buy at least a specified amount of each product per month through government outlets at official prices. A more stringent fixed ration system established in March 1983 remains in affect today, with Cuban-style ration cards distributed by the neighborhood Sandinista Defense Committees. Nonetheless, supplies of these goods have become increasingly scarce, giving impetus to a prospering black market. 25X1 25X1 The regime now uses the block committees and other mass organizations to police neighborhood markets to ensure that official prices are honored, according to the US Embassy. [redacted] 25X1

Shortages are partly caused by inefficient handling and distribution, [redacted] 25X1 For example, [redacted] burdensome customs procedures prevent prompt use of donated goods. Opposition journalists claim regime incompetence is hindering distribution of available supplies of cooking oil and grains. We believe low producer prices drive many farmers to divert goods to the black market. [redacted] 25X1

Nicaragua: Economic Indicators, 1978-85



[redacted] 25X1

308094 2-86

Soaring Food Prices and Declining Real Wages

By early 1985, Managua could no longer afford the huge and growing food subsidies, in part because of escalating military expenditures. [redacted] Citing the drain on the budget and the need to curb speculation, the government sharply boosted official prices for rice, beans, and other staples last February and again on several other occasions during the year—the first substantial increases since 1979. Black-market prices of these goods also rose sharply. [redacted]

The impact of the subsidy cuts on inflation has been tremendous. Between 1979 and 1984, the consumer price index rose by an average of 35 percent per year, according to IMF data. On the basis of US Embassy reporting, we estimate inflation last year at about 300 percent. [redacted] 25X1

25X1

Minimum wages, which were increased by 40 percent soon after the Sandinistas took power, remained virtually frozen for several years despite inflation. Three wage adjustments last year and another hike of 50 to 100 percent in early January did not keep pace with inflation. Analysis of official data indicates that real minimum wages fell by one-third during 1985 alone, while the average purchasing power of all workers dropped by one-fifth last year. Since 1978, real minimum wages have declined by 50 percent and real average wages by two-thirds. [redacted] 25X1

25X1

Nicaragua: Prices for Basic Foods

Cordobas

Product	Unit	Official Prices [a]		Free Market Prices	
		December 1984	December 1985	January 1985	January 1986
Beans	pound	4	105	21	150
Rice	pound	5	21	15	100
Corn	pound	5	10	10	55
Sugar	pound	5	16	7	100
Cooking oil	gallon	60	NA	350	3,000

[a] The current official exchange rate is 70 cordobas per US dollar and the black-market rate is 1,300 per dollar.

[redacted]

Plunging Consumption

US Embassy reporting indicates the steep decline in purchasing power has altered patterns of consumption. The limited data available indicate that per capita consumption of food staples increased in the first two years of Sandinista rule—when food imports were high and prices subsidized—but have fallen steadily since the end of 1981. The plunge in real wages has wiped out savings, restricted the use of private automobiles, dining out, and the purchase of imported goods, and otherwise dramatically altered lifestyles of professionals and the middle class. Minimum-wage earners are postponing purchases of clothing and other basic consumer goods—a pair of pants, for example, costs the equivalent of half a month's earnings. In addition, many Nicaraguan housewives report sharp deteriorations in family diets because of both price and supply constraints. [redacted]

Shortages—even of basic rationed staples—are widespread, despite increased shipments of foodstuffs from the Soviet Bloc last year. Since last Christmas, nearly all basic staples—rice, beans, sugar, cheese, milk, chicken, and meat—have been in extremely short supply in government-run outlets, and cooking oil has been practically unavailable anywhere for several months. According to the US Embassy, this is the first time so many scarcities have occurred simultaneously. While many middle-income consumers are resorting to the black market—where a pound of rice, for example, costs nearly five times the official price—the US Embassy reports that this option is not open to lower income families. [redacted] 25X1

Bleak Prospects

The outlook for consumers remains grim. Several sources indicate the harvest of key staples this year will be significantly lower, in part because of poor growing conditions. Inefficient government economic policies, increased land confiscations, and the growing squeeze on the private sector also are hindering agricultural production. Foreign exchange constraints will limit food imports, although the Soviet Bloc probably will continue to provide enough to satisfy minimum consumption needs. 25X1

[redacted] 25X1

The regime's commitment to eliminate remaining subsidies on consumer goods and foodstuffs—highlighted in an internal government document—probably will push official and black-market prices higher. [redacted] 25X1

The calls by Sandinista leaders for a "survival" attitude in the face of mounting pressures suggest they expect supply problems to continue. Managua is likely to push for more donations from the Soviet Bloc while trying to deflect blame for the shortages to private vendors. The program of land redistribution to bolster support among the peasants will continue. The regime will rely on the expanded state of emergency to prevent strikes, consumer demonstrations, or other manifestations of discontent. Spontaneous reactions may occur, however, as evidenced by the murder of a price control inspector in a Managua marketplace in mid-January as he tried to cite a vendor for price violations. [redacted] 25X1 25X1

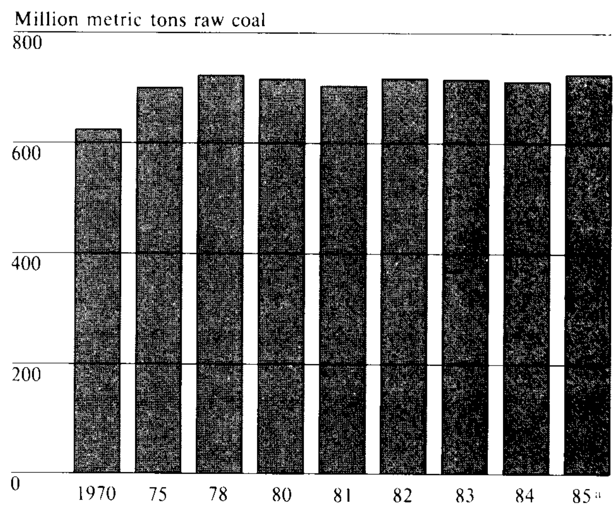
[redacted] 25X1

Declassified in Part - Sanitized Copy Approved for Release 2011/12/08 : CIA-RDP88-00798R000300020005-4

The USSR's Eastern Coal Basins: A Potential White Elephant 25X1

Expanded use of coal underpins the Soviet Long-Term Energy Program; despite this, Moscow's current focus is on oil and natural gas. Planners are counting on coal from eastern deposits, together with nuclear power, to provide nearly all growth in energy output once natural gas production levels off in the mid-1990s. Major problems remain in developing coal-use and energy transfer technologies that will be needed to facilitate expanded coal production in the major eastern basins. Moreover, some of the increased output from these basins will merely offset declining production from the major underground basins west of the Urals. We believe that coal production and utilization will probably increase only slightly—if at all—during the coming decade, leading to energy constraints beginning sometime in the 1990s. 25X1

USSR: Stagnating Coal Production



[a] Peak production.

25X1

308096 2-86

Key Eastern Basins: High Potential for Output . . . and Headaches

The Soviets are banking on the development of selected coal basins in the eastern USSR, but progress in overcoming technical problems related to the transport and use of coal from these basins—Kuznetsk, Kansk-Achinsk, and Ekibastuz—has been slow.

The Soviets have focused largely on their ability to surface-mine vast amounts of coal cheaply, but have underestimated the technical problems and costs of using this very-low-quality coal. To move coal back to the forefront of energy production and use, the Soviets must find and implement technological solutions to two key problems:

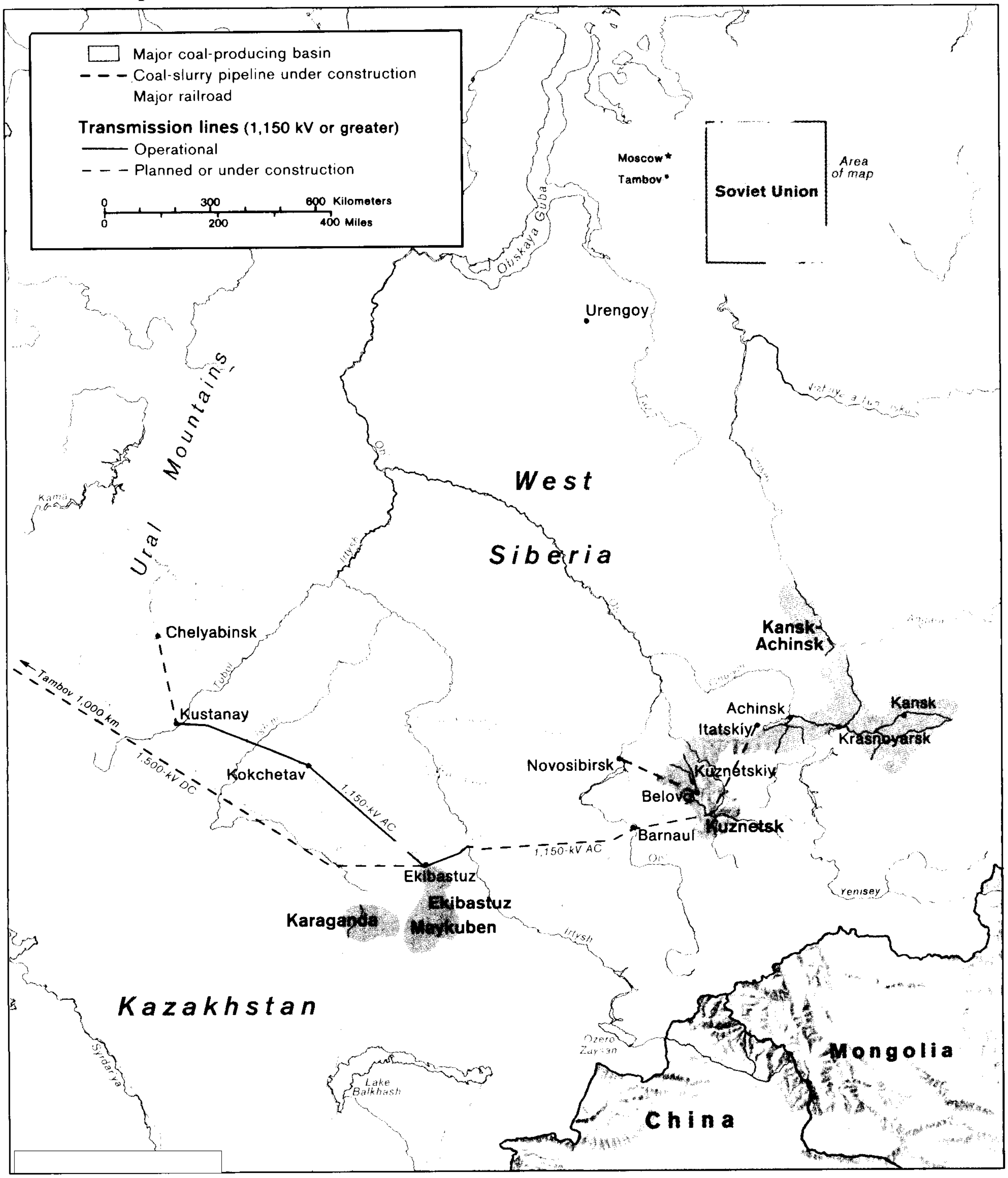
- Low quality of the coal—most of the USSR's coal reserves are low in energy value: either lignites (often with high moisture content) or subbituminous coals with a high ash content. These coals require unique approaches to mining, transportation, and combustion. 25X1

- Distance—the major coal deposits that the Soviets want to develop are thousands of kilometers from the industries and population centers most in need of the energy. Consequently, low-cost energy transportation is essential.

In short, eastern coal may be a white elephant—an energy reserve requiring research and investment funding far out of proportion to the gains achieved by meeting planned targets for coal output and use. 25X1

25X1

Soviet Development of Eastern Coal Basins



707009 (A05636) 2-86

25X1

The key to progress lies in developing state-of-the-art coal-use and energy-transfer technologies—large-capacity lignite-fired boilers, coal-slurry pipelines, ultra-high-voltage electricity transmission systems, and synfuel plants. Mastering these technologies will require carefully planned, well-executed research and development and sizable capital outlays. Annual investment in the coal and power industries would have to increase by 50 percent to provide the estimated 50 billion rubles (roughly $60 billion) required in the next 15 years to successfully fund the planned expansion of coal mining and use.

Because of coal's enormous reserve base and because of dwindling high-quality reserves of oil and eventually even of gas, we judge that the USSR will continue to emphasize coal in its long-term energy plans. It will, however, probably not devote the resources needed in the short term to overcome fundamental obstacles to expanded use. The immediate investment needs of the oil and gas industries and modernization of the machine-building sector during 1986-90 will more likely take priority.

Western Assistance Needed

The inadequacy and slow development of Soviet technology and equipment for coal mining and use have been increasingly criticized by Soviet energy experts in press and industry journals. Some of these specialists have gone so far as to note that Western approaches to the commercialization of coal technology, such as coal liquefaction, are superior to those of the USSR.

If the USSR decides to make the commitment necessary to expand coal output—and is willing to make the hard currency outlays—we believe that Western technology and equipment will play a growing role in the effort and could become major factors affecting the speed and magnitude of Soviet coal development. Coal-cleaning facilities have already been ordered from West German and Italian firms. An Italian firm has recently received a contract to provide process technology and engineering services for a 250-km coal-slurry pipeline to transport 3 million tons of West Siberian coal annually. For the last five years, the Soviets have been soliciting assistance—primarily through technical information exchange agreements—in coal liquefaction technology from Western firms.

25X1

Implications

A failure to expand coal output and use would probably have the following consequences:

- An already tight balance between supply and demand for electric power in the Urals and Kazakhstan would be upset. An increase in the frequency and duration of power shortages during the 1990s would probably lower the output of key metallurgical, defense production, and agricultural facilities in these areas. 25X1

- Many power plants burning coal as their primary fuel would have to continue using more fuel oil than planned because of low coal quality and coal shortages. This situation would hamstring Soviet efforts to free up additional oil for alternative domestic and export uses—an important consideration in view of declining oil output. 25X1

- Shortages of coking coal would continue to be a drag on steel production, adversely affecting Gorbachev's economic modernization program. 25X1

Time is running out on the opportunity to avoid these problems. Moscow could redesign the Long-Term Energy Program and, as an alternative to coal expansion during the late 1990s, attempt further growth in natural gas output and larger-than-expected increments in nuclear energy production. To make these decisions, the Soviet leadership would have to focus on the longer term issues in energy and pull itself away from the day-to-day management that usually occupies its attention. 25X1

25X1

An energy program with greater emphasis on gas and nuclear power would face different but still demanding problems. Further increases in gas output would accelerate depletion of reserves and risk a loss in ultimate recovery, a factor that Gorbachev has already warned against. Moscow is already planning to increase substantially the electricity generated by nuclear power stations in the European USSR. Soviet industry will have to increase considerably the output of nuclear power plant components and equipment if the existing goals are to be met. Nuclear power could not be substituted for coal east of the Urals without even more sizable and costly additions to nuclear-component-manufacturing capacity, major redesign work, and massive training of new personnel.

25X1

LDCs: Obstacles to Foreign Investment [redacted] 25X1

One of the cornerstones of the Baker Initiative is increased inflows of foreign investment into debt-troubled LDCs to compensate for reduced commercial lending and to provide jobs and expertise. Significant increases in such investment are blocked in many LDCs by economic and policy barriers ranging from weak markets to poor investment climates. A number of these barriers could be lowered if LDC governments would adopt some key policy reforms, but the high political costs of the policy actions required will make it difficult for most developing countries to overcome these obstacles over the next few years. Increased foreign investment, in turn, probably will make only a small contribution to the resolution of LDC economic problems. [redacted]

Key Obstacles

Weak Markets. A weak domestic market is a serious barrier to foreign investment in many LDCs, particularly the larger countries. High inflation rates, often coupled with domestic price controls, dampen an LDC's attractiveness by squeezing foreign investor profits when production costs rise faster than sales prices. For example, according to press reports, many prospective foreign firms are postponing investments in Brazil because of a renewed fear of high inflation. Sluggish economies have weakened local markets in Nigeria, the Philippines, and Venezuela as well. These recessions have depressed local demand and reduced domestic purchasing power, temporarily deterring foreign businesses seeking new investment opportunities. [redacted]

The smaller LDCs have a difficult time attracting foreign investors because their domestic markets are limited even in the best of times. Existing local manufacturers frequently have saturated many local and regional markets. This production glut is often magnified by low economic growth and per capita income levels. In Kenya there are limited market niches available to foreign businesses because the domestic market is largely filled with locally manufactured goods and there are few regional marketing opportunities. Similarly, a well-developed domestic consumer products industry in Tunisia precludes foreign investor opportunities in the manufacturing sectors. [redacted] 25X1

Regulatory Environment. Adverse regulatory environments also block foreign investment in LDCs:

- The *restrictive investment codes* of some LDCs deter prospective foreign investors. For example, the Andean Pact countries—Bolivia, Colombia, Ecuador, Peru, and Venezuela—legislate strict foreign ownership and buy-out rules. Even though some of these countries have recently announced legislative improvements, investors are still reluctant. Similarly, Mexican legislation that restricts overseas ownership to a minority position and enforces local content conditions in the automotive and pharmaceutical industries is a key disincentive to foreign firms, although notable exceptions have been made for large-scale projects. 25X1

- *Inadequate legislative safeguards* to protect patents and intellectual property have discouraged many high-technology businesses from entering into overseas ventures. South Korea's patent laws, for example, protect only the manufacturing process, not the product. Similarly, Argentine patent protection is weak to nonexistent in many sectors, especially in the pharmaceutical industry, according to Embassy reporting. 25X1

[redacted] 25X1

Developing Countries: Obstacles to Foreign Investment

✱ Serious obstacle ● Moderate obstacle Minor obstacle

	Weak markets	Regulatory environment	Political instability	Bureaucratic delays	Foreign exchange
Argentina	●	●		●	●
Brazil	●	●			
Chile	●		●		
Colombia	●	●			
Ecuador	●			●	
Egypt	●	●		●	●
Honduras	●			●	●
Jamaica	●		●	●	●
Kenya	●	●		●	
Mexico	●	●		●	●
Nigeria	●	●	✱	●	●
Pakistan	●	●	●	●	●
Peru	●	●	●		●
Philippines	●	●	✱	●	●
South Korea		●			
Sudan	●	●	✱	●	●
Tunisia	●		●		
Venezuela	●	●		●	

The extent of the obstacles blocking foreign investment varies across LDCs. The constraints are most severe in Nigeria, the Philippines, and Sudan. For these LDCs, the uncertain domestic political situation is the most serious obstacle, but foreign investors also face moderate barriers in other areas. Constraints are also large in Egypt and Mexico. On the other hand, South Korea poses the fewest obstacles to foreign investors, with the regulatory environment, especially poor intellectual property right protection, serving as the only major constraint to overseas ventures.

[redacted] 25X1

308095 2-86

- The *preferential treatment* of domestic firms—through subsidies, assured access to local inputs, and guaranteed market shares—also deters foreign investment. These benefits—most prevalent in LDCs with centralized, highly state-controlled economies—give the local firm, often a parastatal, an advantage over foreign firms. In Egypt, for example, the subsidized sale of energy only to parastatals places foreign investors at a disadvantage. Similarly, in Pakistan controlled prices, coupled with growing local-content requirements, are likely to reduce the profits of foreign-owned businesses. [redacted] 25X1

Political Uncertainty. A third major obstacle is an uncertain domestic political environment. Overseas firms are cautious when considering an investment in an LDC faced with an insurgency problem—such as the Philippines, Colombia, and Peru—because of the greater chance of losing their assets under chaotic conditions. Similarly, the possibility of a change in government, whether by an election or by coup, may deter the entry of foreign investors until the policy position of the new regime is clear. In LDCs with elections pending—the Philippines, Jamaica, and Chile—or in countries with a history of coups, such as Nigeria, foreign investors are likely to adopt a wait-and-see attitude. In addition, the potential for a spillover of regional tensions may deter some foreign investors from considering such LDCs as Egypt or Honduras. [redacted]

Bureaucratic Delays. A lengthy and cumbersome approval process is the fourth major constraint. This difficulty is often compounded by a review of the application by government ministries that have no jurisdiction over the business or that have little authority to make decisions. These delays create added expense for foreign investors and prevent them from taking advantage of favorable market conditions. Bureaucratic delays have been cited as a moderate disincentive in Egypt, Nigeria, Pakistan, the Philippines, and Venezuela. [redacted]

Foreign Exchange Difficulties. Chronic problems in gaining access to foreign exchange also discourage overseas investors. Foreign exchange shortages may create delays in receiving the foreign currency necessary to import equipment or materials needed for production, making it difficult for foreign investors to operate efficiently in many LDCs. Such delays are a problem for foreign investors operating in Argentina, Mexico, Nigeria, and the Philippines. In addition, when foreign currency reserves dwindle, LDC governments often tighten controls on profit remittances, as has happened in the Philippines, Argentina, and Nigeria. [redacted]

An overvalued exchange rate, usually a source of difficulty in obtaining foreign exchange, also discourages foreign investors directly. Since many potential investors rely on imports for productive inputs and export markets for sales, an overvalued exchange rate implies a smaller return on foreign investment. The overvalued currency also penalizes foreign firms by distorting profit repatriation and reinvestment levels. [redacted] 25X1

Needed Policy Reforms

We believe that government policy reform in three key areas could offset some of these obstacles and lead to a dramatic improvement in the investment climate in these LDCs over the medium term:

25X1

- *Improving the regulatory environment.* Actions that open new sectors to foreign firms can be a major step in attracting overseas investors, especially in high-growth industries. South Korean reforms in 1984 and 1985 that permit foreign ventures in recently opened sectors and Argentine efforts to attract foreign businesses in order to spur technology transfer are prime examples of LDCs loosening regulatory obstacles. Also important in attracting new foreign firms are regulatory measures to protect patents and other intellectual property and actions to equalize government preferential treatment.

25X1

- *Overhauling the investment approval process.* Most important are efforts to simplify the approval process by centralizing the authority to consider and provide all the permits necessary for prospective investors to begin operation. Egypt, in October 1984, adopted new measures to streamline the bureaucracy by allowing the Investment Authority to grant provisional approval to a project the day of submission. Another example is the July 1984 Foreign Capital Inducement Law in South Korea that now permits automatic approval of foreign investment applications for projects that meet size, export, and ownership criteria.

25X1

- *Reforming the foreign exchange system.* Where exchange controls exist, reforms are necessary to ensure that adequate foreign exchange currency

Selected LDCs:
Net Foreign Direct Investment Flows

Million US $

	1980	1981	1982	1983	1984	1985
Argentina	788	944	257	183	268	350
Brazil	1,544	2,313	2,534	1,373	1,556	1,500
Chile	170	362	384	148	67	65
Colombia	51	228	337	514	411	250
Ecuador	70	60	40	50	50	60
Egypt	541	747	285	471	713	850
Honduras	6	−4	14	21	8	10
Jamaica	28	−12	−16	−19	0	10
Kenya	80	60	82	50	54	50
Mexico	2,186	2,537	1,655	459	391	450
Nigeria	−734	543	430	345	200	200
Pakistan	59	107	66	31	61	50
Peru	27	125	48	38	−89	−100
Philippines	−106	172	16	105	−6	−25
South Korea	−7	60	−76	−57	73	125
Sudan	0	0	0	0	9	0
Tunisia	235	291	339	186	115	175
Venezuela	55	184	253	86	42	75

[redacted] 25X1

is available to foreign investors. In countries with severe payments problems, allocation may be necessary to provide faster and more reliable access to exporters or designated firms. Jamaica, for example, now uses an auction system to allocate and distribute its scarce foreign exchange. Also important is the correction of overvalued exchange rates, which removes the export disadvantage facing many foreign-invested companies. [redacted]

High Costs Will Limit Reform

Whether an LDC government will undertake these policy actions will depend on the results of a careful weighing of costs and benefits—both political and economic. On the one hand, the entry of foreign investment could greatly increase output and accelerate economic growth and development. In addition, a foreign investor may also help ease foreign payments pressures, expand the country's export capabilities, spur technology transfer, and reduce domestic unemployment problems. Better bilateral political relations and additional commercial financing also may follow from LDC efforts to remove obstacles to foreign investment. [redacted] 25X1

25X1

In contrast, there are economic and political costs in changing policies to attract foreign investment that limit the scope of investment reform. The economic costs associated with reform efforts are generally minor, however: local unemployment may rise as a result of greater competition from foreign firms; and the prices of imports are likely to increase after a devaluation, possibly heightening current account pressures and fueling inflation temporarily. [redacted] 25X1

The greater constraint is the high political costs. Vested interests—some local producers, the military, government elites, and the bureaucracy—often oppose improving investment regulations because they would suffer reduced profits or a perceived loss of control over the economy by liberalizing foreign investment regulations. Because of their political power, their opposition is often effective. For instance, the Argentine bureaucracy, in order to maintain economic control over oil production and revenues, delayed many of the March 1985 regulatory reforms proposed for the petroleum industry, according to Embassy and press reporting. Because new foreign investors would be competitors in the limited local market, local producers also may reject investment reform. In Mexico, for example, pressure from two existing computer joint ventures was a major factor in the rejection of IBM's initial proposal, according to the assessment of one source. [redacted] 25X1

Implications

In the face of these domestic political costs, LDC efforts to reform investment regulations will be quite limited, in our view. Moreover, we expect many of the other major obstacles inhibiting foreign investors to remain, thus minimizing the favorable impacts of any reforms and reducing the chances of an increase in foreign investment in the LDCs. Indeed, the flow of foreign investment into developing countries over the short term will probably stay well below historical highs and have only a limited impact on generating new economic growth, replacing lost commercial borrowing, easing foreign payments problems, or transferring technology. [redacted] 25X1

[redacted] 25X1

Declassified in Part - Sanitized Copy Approved for Release 2011/12/08 : CIA-RDP88-00798R000300020005-4

Stagnant Caribbean Exports: Continuing Drag on the Regional Economy [redacted]

25X1

Despite access to preferential trade arrangements, such as the Caribbean Basin Initiative (CBI), Caribbean exports continue to decline, both to the United States and other developed countries.[1] Weak markets for the major commodity exports—particularly petroleum—are the principal problem, but inadequate government policies to promote exports and investment, and currencies pegged to a still relatively high US dollar have also contributed to poor export performance. Declining exports are hurting the region's domestic economies and their effects are exacerbating political problems. At the same time, the depressed state of the Caribbean economies is encouraging drug production and trafficking, directed largely toward the US market. As a result of their difficulties, these countries most likely will continue to ask for increased US assistance and market access, especially for sugar and apparel. [redacted]

Exports to the United States: Still Declining

While the United States remains the Caribbean's largest trading partner, exports from the region to the United States fell by over 17 percent between 1980 and 1984, according to US trade data, and continued to decline in 1985. Hard-hit Caribbean exports include some of the region's most important revenue-earning commodities—bauxite, petroleum, and sugar. Moreover, tourism—usually a high revenue earner—was also down last year. [redacted]

[1] Caribbean export statistics are based on industrialized country import data. In this article, the Caribbean area includes the following countries: Anguilla, Antigua, The Bahamas, Barbados, Bermuda, British Virgin Islands, British West Indies, Cayman Islands, Dominica, Dominican Republic, Grenada, Guadeloupe, Haiti, Jamaica, Martinique, Montserrat, Netherlands Antilles, St. Christopher and Nevis, St. Lucia, St. Pierre and Miquelon, St. Vincent, Trinidad and Tobago, and Turks and Caicos Islands. Not all of these nations are members of the trade programs or organizations that are discussed. [redacted]

Caribbean fuel exports to the United States suffered the largest drop, declining from $6.3 billion in 1980 to $4.3 billion in 1984. The Bahamas, Netherlands Antilles, and Trinidad and Tobago were especially hurt by the decline in fuel exports. In contrast, exports of manufactures increased by about 80 percent, rising to $1.4 billion. The shift was due, in part, to increased US demand for chemicals, clothing, and electrical machinery. [redacted]

25X1

Exports to the European Community: Falling Even Faster

Caribbean exports to the EC have also declined in the 1980s, dropping by 40 percent from 1980 to the 1984 level of $1.6 billion. EC imports from the region during the first three quarters of last year, however, were 9 percent higher than the same period in 1984. On a commodity basis, sales of fuels to the EC fell from $1.8 billion to $900 million between 1980 and 1984. Caribbean food exports to the EC also declined, falling 12 percent to $500 million between 1980 and 1984; hardest hit were Jamaica, Haiti, the Dominican Republic, and Trinidad and Tobago. [redacted]

25X1

25X1

As with the CBI, the Lome Convention—an EC preferential trade, aid, and credits program for some 66 African, Caribbean, and Pacific (ACP) countries—has met with only limited success in the Caribbean. Caribbean participants have failed to benefit under Lome because they lack entrepreneurial initiative and maintain overvalued exchange rates, according to the EC's Caribbean representative. Both the EC and the ACP countries also agreed that much aid in the past was used inefficiently. Although the latest Lome renewal

25X1

25X1

Caribbean Countries: Exports to the United States and the European Community

Million US $

	1980		1982		1984		1985 [a]	
	US	EC	US	EC	US	EC	US	EC
Total	**8,221**	**2,742**	**6,386**	**2,164**	**6,800**	**1,637**	**3,829**	**1,056**
Netherlands Antilles	2,679	636	2,186	663	2,098	535	689	233
Trinidad and Tobago	2,449	426	1,667	491	1,411	304	1,003	194
The Bahamas	1,433	927	1,086	338	1,218	120	531	164
Dominican Republic	769	77	616	58	921	66	801	49
Jamaica	418	236	323	174	415	125	239	107
Haiti	264	88	325	64	394	61	304	50
Other	209	352	183	376	343	426	262	259

[a] First three quarters.

Source: UN and IMF trade statistics.

[redacted] 25X1

attempts to ensure more effective development-oriented use of aid, we doubt these efforts will be successful in the short term. [redacted]

Several ACP states argue that greater access for agricultural exports to the EC—currently limited by the EC Common Agricultural Policy—is the key to rapid export growth. ACP access for most agricultural products is generally no better than access provided to other countries outside of the agreement, and the EC is unlikely to liberalize its agricultural trade policy. Although there are special arrangements for sugar, rum, and bananas, exports of these products to the EC, except for bananas, declined sharply during the 1980s. [redacted]

Intra-Caribbean Trade: Low and Continuing To Fall

Trade within Caricom [2] also has declined over the past four years, falling by about 25 percent from 1981's record level of $540 million. Trade fell a further 10 percent for the first three quarters of 1985 as compared to the same period in 1984. [redacted] 25X1 25X1

Foreign payments problems in most countries in the region, combined with the failure of some Caricom members to remove various tariff and nontariff barriers, have contributed to the decline in intracommunity trade. Reacting to the decline in petroleum prices, Trinidad and Tobago—Caricom's largest regional market—attempted to reduce imports and stem a decline in foreign exchange by instituting import licensing. Most recently, it devalued its currency by one-third. Although Port of Spain agreed last month to remove import licensing in response to complaints from its Caricom neighbors, Barbados announced limited retaliatory measures against selected Trinidadian goods. [redacted] 25X1 25X1

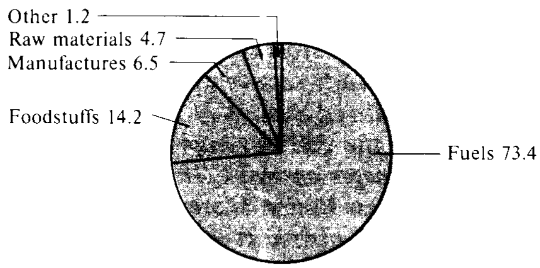
Despite commitments to expand intracommunity-trade at the past two Caricom Heads of Governments Conferences, members have been slow to act. An agreement—the Nassau Understanding—

[2] The Caricom countries—the Caribbean Economic Community—include Anguilla, Antigua, The Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, Montserrat, St. Christopher and Nevis, St. Lucia, St. Vincent, and Trinidad and Tobago. [redacted] 25X1

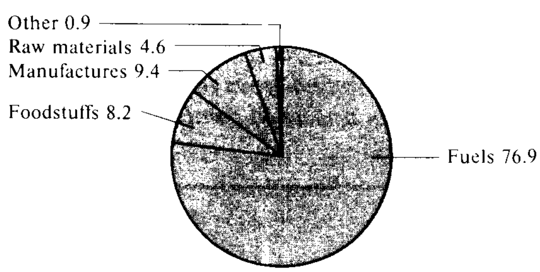
United States: Commodity Composition of Imports From the Caribbean

Percent

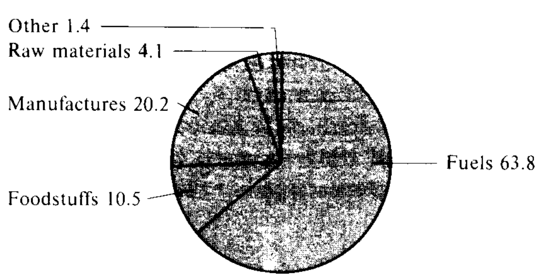
1975
US $4.7 billion



1980
US $8.2 billion



1984
US $6.8 billion

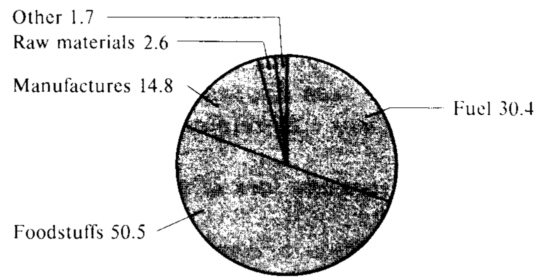


308116 2-86

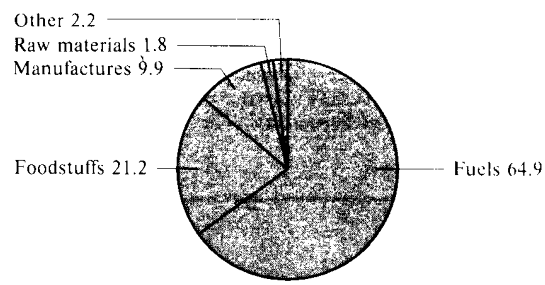
European Community: Commodity Composition of Imports From the Caribbean

Percent

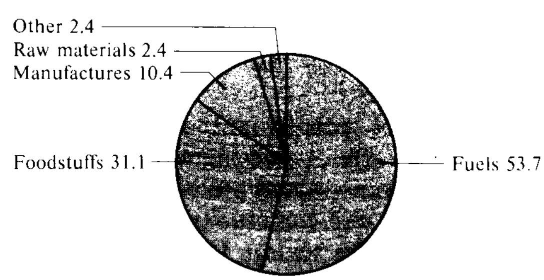
1975
US $1.2 billion



1980
US $2.7 billion



1984
US $1.6 billion



308117 2-86

25X1

25X1

Caribbean Basin Initiative: Limited Success

The Caribbean Basin Initiative (CBI)—a unilateral free trade arrangement between the United States and designated Caribbean Basin countries implemented in late 1983—is intended to stimulate investment in nontraditional export industries, create jobs, and foster political and social stability in the region.[a] *Preliminary trade results under the CBI, however, have been disappointing. Several factors have held back CBI-related export development, including:*

- *Poor infrastructure and lack of sufficient manufacturing capacity.*
- *Continued dependence on commodity exports experiencing depressed prices—for example, sugar, bauxite, and bananas.*
- *Inadequate government incentives to expand investment and increase export competitiveness.*
- *Many currencies pegged to the US dollar.* [redacted]

From the Caribbean perspective, the CBI is viewed as too limited because it excludes key exports—textiles, apparel, footwear, and petroleum—where these countries have a comparative advantage, and because CBI-eligible exports make up only 7 percent of total US imports from the designated Caribbean countries. Most of the items included under the CBI already receive duty-free access under the Generalized System of Preferences (GSP), although the CBI has improved rules of origin and eliminates annual GSP product reviews and competitiveness limits. Moreover, US sugar import quotas have also hurt low-cost Caribbean sugar exporters. Caribbean and Latin American sugar-exporting countries asked the United States during an OAS Permanent Council meeting last month to reconsider the reduction in sugar quotas. Secretary General Rainford of the Caribbean Economic Community (Caricom) stated last July that the CBI has failed to achieve balanced economic development in the region, and he has requested a review of the CBI to find ways to ensure that the program's benefits accrue to smaller countries. [redacted]

25X1

25X1

[a] *The Caribbean CBI countries include Anguilla, Antigua, The Bahamas, Barbados, British Virgin Islands, Cayman Islands, Dominica, Dominican Republic, Grenada, Haiti, Jamaica, Montserrat, Netherlands Antilles, St. Christopher and Nevis, St. Lucia, St. Vincent, Trinidad and Tobago, and Turks and Caicos Islands.* [redacted]

25X1

drafted in 1984, but not yet fully implemented, proposes to:

- Remove all barriers to free trade in Caricom.
- Establish a common external tariff to protect a selected group of products made in Caricom countries.
- Increase domestic content requirements for goods seeking duty-free entry from the Leeward and Windward Islands.

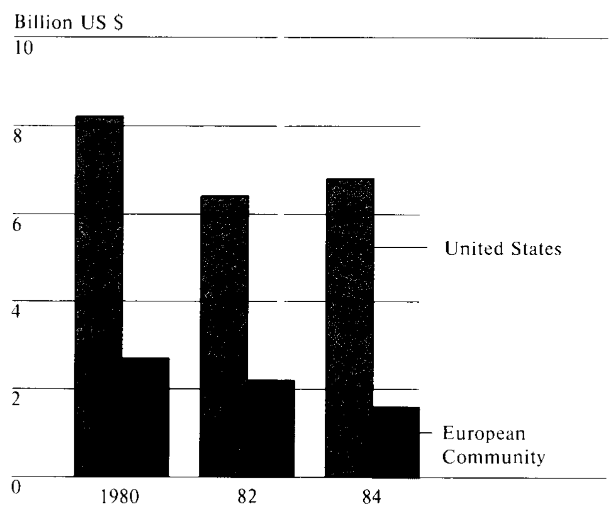
The agenda for the recently postponed Caricom Council meeting—the second-highest decisionmaking body in Caricom—would probably have included a discussion on intracommunity trade, including implementation of the Nassau Understanding, according to press reports. [redacted]

25X1

Outlook

No rebound in Caribbean exports is likely in the near future. Export growth will continue to be restrained by dependence on low-priced commodities, poor infrastructure, and insufficient government export incentives. While the CBI has stimulated some export diversification—manufactures' share of total Caribbean exports to the United States more than doubled to about 20 percent between 1980 and 1984—exports to the EC probably will remain concentrated in fuels and foods.

Caribbean Exports to the United States and the European Community



308115 2-86

Caribbean Drug Trafficking

Located between South American sources of cocaine and marijuana and the US market, the Caribbean has become one of the world's leading transshipment areas for narcotics. According to reporting from US Embassies in the region, the continued recession in the Caribbean economies has provided strong incentives to replace lost income through drug smuggling. In Jamaica—the only major producer of illicit drugs in the Caribbean—a joint military/police task force is struggling to suppress a deeply entrenched drug industry that directly employs an estimated 25,000 agricultural laborers, and many more in indirect employment. In The Bahamas, drug smuggling has created pervasive corruption. Finally, US law enforcement pressure on customary smuggling routes appears to be pushing traffickers to develop new transportation channels through Haiti, the Dominican Republic, and the islands of the eastern Caribbean. 25X1

25X1

Trade within Caricom will most likely continue its decline or become stagnant as long as these countries face domestic economic problems and attempt to restrict imports.

The adverse impact of stagnant trade on the Caribbean will continue to spill over into Caribbean political affairs. Continued discontent and protests from the public and private sectors over worsening economies, as well as the need to increase exports and foreign exchange earnings, will probably be major issues in the region's upcoming elections—for example, in Jamaica, Barbados, and the Dominican Republic. Poor economic prospects also are encouraging drug production and trafficking, with much going to the United States. As a result, Caribbean leaders probably will call for increased US assistance and market access, including an expansion of the CBI program, especially in sugar and textiles. 25X1

25X1

25X1

Declassified in Part - Sanitized Copy Approved for Release 2011/12/08 : CIA-RDP88-00798R000300020005-4

Briefs

Energy

UK Choices on Oil Production

British officials continue to assert that they will not agree to OPEC calls to limit oil production, but London may take subtle steps to influence North Sea producers if prices fall much further. Prime Minister Thatcher told Parliament last week that output levels remain in the hands of the producing companies. The British realize that their small share of output has little leverage on world oil prices. Moreover, the British are convinced that OPEC stands to lose more from an oil price war than the United Kingdom, with its more diversified economy. Nevertheless, if OPEC took concerted steps to offset a sharp fall in oil prices, London probably would quietly move to support OPEC actions by encouraging producers to delay some pumping until prices recover. [redacted] 25X6

Indonesia's New Marketing Strategy Hits Snag

Jakarta's plan to restructure its marketing strategy to cope with declining oil prices has stalled, according to US Embassy reporting. A new reference price scheme based upon a market basket of crudes would result in an immediate loss of tax revenue. Moreover, a change in the present system would adversely affect liquified natural gas revenues because some LNG contracts are based on the government's selling price for oil. [redacted] 25X1 Until these matters are resolved, foreign firms will continue to resist pleas by Indonesian officials that they boost production. Under the existing pricing arrangement, the production share of oil companies—contractually set at 15 percent—has been reduced to below 10 percent. Although the government will not publicly admit it, total oil production is in slow decline, and further development of existing fields is unlikely in the present investment climate. [redacted] 25X1

Angolan Oil Production Rising

Angola's oil production will increase by 30 percent during 1986 to 300,000 b/d [redacted]. Oil exports last year earned $1.8 billion, 25X1 more than 90 percent of Angola's hard currency receipts. Luanda spent about half of its 1985 oil earnings for Communist military assistance to support the fight against UNITA insurgents. If prices stay at current levels—about $20 a barrel, as compared with roughly $25 a barrel in 1985—Angola will earn as much as $2 billion in hard currency from oil exports in 1986. Luanda again in 1986 will have to allocate [redacted] earnings from oil sales to 25X1 Communist countries to support its military effort and to service debts. [redacted] 25X1

India Rolls Back Domestic Oil Price

The government this week was forced to roll back some of the 1 February petroleum product price increases. The initial increases ranged from 5.6 percent on diesel fuel to 20 percent on liquid petroleum gas. Apparently all the price hikes except for aviation fuel have been trimmed. Over the last 15 years the annual growth in oil demand has exceeded 5 percent and growing sales of automobiles and other vehicles have probably pushed growth up to about 7 percent the past year. The new prices met with opposition from the members of the ruling party as well as industry and trade associations. About 2,000 people were arrested in New Delhi early this week following a protest over recent price hikes on a variety of essential consumer goods, including petroleum products. The attempt to boost the price of kerosene, in particular, will probably be exploited by critics of Prime Minister Gandhi's economic policies as more evidence of discrimination against the poor. [redacted] 25X1

International Finance

Soviet Gold Sales

Following a substantial rise in Soviet gold sales last year, Moscow may be scheduling a further increase this year. [redacted] 25X1 Annual net Soviet gold sales have been estimated at less than 100 tons from 1982 to 1984, but the estimate is 180 tons for 1985. With oil output and prices declining, and a sluggish arms market, higher gold sales—possibly as much as the 300 to 400 tons sold annually in the mid-1970s—would ease Moscow's hard currency situation. The USSR is likely to proceed with its customary caution, however, to guard against a fall in the price of gold. Sales to nontraditional buyers, such as Japan, might give Moscow greater latitude to sell gold without depressing prices. [redacted] 25X1

[redacted] 25X1

25X1

[redacted]

Tanzanian-IMF Talks Falter

Negotiations between the government and the IMF lapsed this week because of conflicts over devaluation, mismanagement of semiofficial enterprises, and low prices for commodities. [redacted] Military interference in the government remains an unlikely prospect, but the Army and civil service appear increasingly frustrated by the economic deterioration and Nyerere's continued influence. [redacted] 25X1

25X1

IMF Declares Khartoum Ineligible

The IMF Governing Board's decision to declare Sudan ineligible for Fund resources will have little effect on the country's already bleak economic outlook. The action follows over a year of unsuccessful attempts by Khartoum to negotiate an acceptable economic reform package and a resolution of arrearages to the Fund, which currently total over $200 million. Last minute attempts by the regime to forestall the IMF action, including a reported $10 million arrearage payment last week, were insufficient to alter the IMF decision. The declaration of ineligibility does not prevent further consultation between the IMF and Khartoum, nor does it actually change Sudan's access to Fund financial resources—Khartoum has been effectively barred from IMF resources from the moment that arrears began in July 1984. The formal declaration will, however, probably be viewed by the Sudanese as a slap in the face from the United States and other Western benefactors and may provoke an anti-US reaction. [redacted] 25X1

Global and Regional Developments

EC Unemployment Continues To Rise

Unemployment in the EC-10 for 1985 continued its upward trend, rising from 12.4 million persons to almost 13 million—or just over 11 percent of the labor force. The increase was largely the result of a rise in female unemployment, which rose from 11.4 percent in 1984 to nearly 12 percent last year; male unemployment edged up only slightly to 10.2 percent over the same period. The trend in joblessness was not uniform in the member states, with the four major countries and Ireland showing increases while the remaining five countries posted decreases. EC governments are continuing to concentrate on reducing inflation to boost real incomes, and, with the help of declining oil prices, they are anticipating an improvement in economic growth that could halt the rise in joblessness. [redacted] 25X1

25X1

National Developments

Developed Countries

Pressure Building on Ottawa To Reduce Deficit

Ottawa is unlikely to meet demands from the business community for drastic budget cuts. Faster-than-anticipated economic growth and—until recently—lower interest rates may enable Ottawa to achieve its goal of a US $1.3 billion reduction in the fiscal 1985/86 deficit. Business groups, however, have used the recent decline in the Canadian dollar to bolster arguments that additional spending cuts of at least $3.5 billion are needed this year to reassure financial markets. Finance Minister Wilson has publicly admitted that his new budget, expected in late February, must demonstrate the political will to get spending under control. Despite the Finance Minister's rhetoric, and a deficit still above 7 percent of GNP, Prime Minister Mulroney has been reluctant to risk the unpopularity such sharp reductions might bring. In a yearend interview, Mulroney ruled out spending cuts of the magnitude the business lobbies desire. We believe the next budget will propose a deficit reduction package of, at most, $1.4 billion, and will probably rely on higher taxes to accomplish even this modest goal. 25X1

Pressure on the Canadian Dollar

Ottawa is concerned that its efforts to prop up the Canadian dollar will undercut economic growth, and it is becoming less inclined to defend the currency. The government's attempts over the past six weeks to strengthen the dollar by raising interest rates and intervening in exchange markets have slowed but not stopped the decline. The drop is caused by the negative effects of falling oil and gas prices on a trade surplus that was already declining and by the financial market's lack of confidence in Prime Minister Mulroney's willingness to further cut spending in the coming budget. The government's focus of concern has switched, however, to the effects of higher interest rates.

For now, Ottawa will probably maintain higher rates while hoping firmer oil prices and a more austere budget will provide relief. If this policy works, the government will gradually reduce interest rates, thereby accepting a weaker currency but promoting higher growth. 25X1

25X1

Tokyo Plans To Restructure Refining Industry

In an apparent move to liberalize petroleum product imports, MITI has announced plans for a private industry group—the "oil vitalization industry center"—to oversee the voluntary reduction of oil refining capacity by 20 percent over the next three years, according to the US Embassy. The Ministry has proposed that Japanese companies be given financial assistance totaling $25 million in fiscal 1986 (beginning in April) to scale down or scrap existing refining facilities. Although awaiting final details, firms in the financially troubled industry probably will take advantage of the Ministry's restructuring plan. Nonetheless, the project would not completely eliminate excess domestic capacity—refining capacity currently is about 5 million b/d, 35 percent above domestic demand. 25X1

25X1

British Unemployment Worsens

Unemployment climbed again in January, dashing London's hopes that joblessness had peaked in mid-1985. The seasonally adjusted total rose by 20,600 last month to a record high of over 3.2 million people, or 13.2 percent of the labor force. The news coincided with an OECD assessment that Britain's unemployment problem appears more persistent and deep-rooted than in the 1930s. The report supports conclusions from other recent studies that excessively high wages are at the core of the problem. The government—relatively complacent about unemployment in recent months—now faces heightened pressures for direct action to combat unemployment in the upcoming March budget. Conservative MPs and the Confederation of British Industry are demanding that the Treasury use any discretionary money in the budget—already limited because of falling oil prices—to create jobs directly rather than go through with even scaled-down tax cuts. The Thatcher government will probably continue to reject both direct jobs programs and any formal incomes policy and emphasize easing labor market rigidities. [redacted] 25X1

Britain Involving Private Sector in Urban Renewal

A housing and planning bill introduced last week seeks to enhance the private sector's role in the regeneration of inner city areas. If passed, the legislation will clear the way for the government to circumvent local authorities and give financial aid—about $28 million per year—directly to specific projects in the most deprived urban areas. The Tory government believes that many of the Labor-controlled local councils have not fully utilized past grants because of ideological bias against the private sector. The proposed legislation also aims to eliminate much of the cumbersome local planning bureaucracy. While inner city programs are targeted to be cut somewhat in the 1986-87 budget, Environment Secretary Baker hopes his initiative will persuade the Treasury to provide new money. The new legislation may help secure a longterm commitment of private developers and financial institutions to inner city problems. At the very least, it will be used to rebuff charges that Prime Minister Thatcher is "uncaring." [redacted] 25X1

Italian Efforts To Join G-5

Prime Minister Craxi wrote letters to each of the G-5 countries last month pressing them to support Italy's membership in the group, and he seems certain to raise the issue at the Tokyo Economic Summit in May. [redacted] 25X1 Craxi's push is probably based on a desire to share in the increasing international press attention generated by the G-5 meetings. According to the press, France supports Italy's bid. Other G-5 members appear willing to consider Craxi's request, but are in no hurry to act on it. [redacted] 25X1

Business Booming for Netherland's Fokker

Fokker is having increasing success with its new F50 and F100 passenger aircraft designs and may move in the next year on a third new model, a derivative of the F100. After a number of lean years, the two new advanced commuter aircraft are being bought in large numbers by prestigious airlines. The 50-seat F50 now has 38 firm orders from six airlines plus 12 options, and the 100-seat F100 has 38 firm orders from three airlines with 31 options. Recent customers include Swissair and US Air. Fokker's marketing strategy is focusing on larger, established airlines in the United States and Western Europe that account for as much as 85 percent of the market. Production rates for the F50 are planned to reach 25 aircraft per year and, for the F100, 36 aircraft per year. 25X1

Sweden's Centralized Wage Negotiations Unsuccessful

The Palme government has failed to obtain business and labor agreement for wage restraint in the current round of nationwide negotiations. Stockholm has been pushing wage restraint in an effort to control costs and improve export performance. In 1984, centralized negotiations also broke down—the first time in three decades—and the recent failure reveals continued strains in the process. This round was broken off by the Swedish Employers' Federation, which represents most private-sector employer associations, on the ground that wage demands by both the blue- and white-collar organizations were excessive. They were also concerned that the government would preempt the bargaining process and dictate an incomes policy. Some unions also rejected the government's call for wage restraint outright because of the low unemployment rate and last year's decline in real income. 25X1

Less Developed Countries

New Nicaraguan Devaluation

The Sandinistas devalued the currency by 60 percent on 31 January, fixing the cordoba at 70 to the dollar for most transactions. Embassies and nontraditional exporters, however, will be able to convert one-fourth to one-half of their foreign exchange at 750 cordobas to the dollar. This second steep devaluation within the past twelve months still fails to offset the triple-digit inflation. The black-market value of the cordoba, now about 1,300 to one, is likely to continue to fall. Increased cordoba receipts are still unlikely to cover costs for many exporters, while private-sector importers will see their already limited access to imports further constrained. 25X1

Panamanian Austerity Proposals

Economic reforms proposed this week by President Delvalle probably will not go far enough in meeting foreign lenders' requirements and are already prompting opposition at home. After four months of indecision, the President announced proposals for labor reform but indicated he would not trim government spending or remove subsidies for industry. The labor coalition immediately announced it would organize protest demonstrations. Delvalle's proposals are an important first step but his failure to address industrial protectionism and a budget deficit caused by a bloated public sector is likely to hinder progress in negotiating a financial rescue package. 25X1

Dominican Republic Eases Austerity

The Dominican Republic is relying on increased coffee earnings to partly finance public-sector wage hikes while continuing compliance with IMF guidelines for the final drawing in April on a $78 million standby loan. The US Embassy reports that coffee earnings—roughly 10 percent of total 1985 exports—could grow by $90 million this year. Public-sector workers had threatened strikes and violent protests if 1985 wage increases were rescinded this year. Last year the government liquidated reserves of a state-owned gold mine to meet the payroll while still meeting IMF targets. Nonetheless, there is a danger that President Jorge Blanco will cite better coffee prices as a reason for relaxing economic austerity before the May presidential elections. Entrenched problems, such as inflation and the weak sugar market, continue to plague the economy, and if the government eases fiscal discipline too far, economic recovery may well elude the next administration. [redacted] 25X1

[redacted]

25X1

Labor Troubles Continue in Moroccan Phosphate Sector

The four-week-old strike at the state-owned Youssoufia phosphate mine shows no sign of ending. [redacted] some 5,000 workers are participating in the walkout largely over recognition of their union. Workers also are protesting the arrest of several of their leaders, the firing of nearly 50 miners for union-related activities, and harassment by local authorities. Embassy reporting indicates the strike will not have a serious impact on the production of phosphate—Rabat's primary export commodity—unless it spreads to other mines. Moreover, the Youssoufia mine has large stocks of phosphate on hand. According to the Embassy, security forces believe they are capable of controlling any outbreaks of violence that may occur. [redacted] 25X1 25X1

Tunisian Corruption Reverberations

Corruption has become a major issue as Tunis sets the stage for a new round of austerity. Unlike previous anticorruption efforts, this campaign has the personal backing of President Bourguiba, who has vowed to spend his final years rooting out social evil, according to the US Embassy. In support of his vow, Bourguiba threatened to divorce his wife, discharged his son from public office, and jailed longtime labor boss Habib Achour and the head of Tunis Air.

Nevertheless, Bourguiba probably will make amends with senior officials implicated in corruption because of their close ties to Tunisia's powerful family clans. Sparing high officials almost certainly will exacerbate public cynicism regarding the regime and its call for greater public sacrifice. [redacted] 25X1

Commercial Crackdown in Syria

The government has undertaken a wide-scale crackdown on illegal money changing and smuggling. As many as 1,500 money changers have been arrested throughout Syria, according to the US Embassy, and the Lebanese border has been closed to all but official travel. [redacted] 25X1 The pound has temporarily strengthened to about 16 to the dollar—a 25-percent improvement—but the Syrian moves are likely to increase rather than mitigate inflation in the long run. [redacted] 25X1

Tanzanian Coffee Offers Little Hope

Tanzania will reap only limited benefits from recent increases in world coffee prices, despite a bumper 1985 crop estimated to be more than 10,000 metric tons above 1984's yield. Acute shortages of fuel and gunny sacks have stalled the delivery of coffee to processing plants and ports, according to US Embassy reporting. In addition, higher prices and the lure of immediate payment have led many Tanzanian growers to smuggle coffee into Burundi and Kenya. The Embassy estimates that over 3,000 tons—about 5 percent of last year's crop—have disappeared into neighboring countries. Moreover, the government has seized foreign exchange earmarked for the purchase of agricultural chemicals vital for future plantings; consequently, some 20 percent of next year's crop could be lost as a result of insects and disease. [redacted] 25X1

Pakistani Finance Minister Dismissed

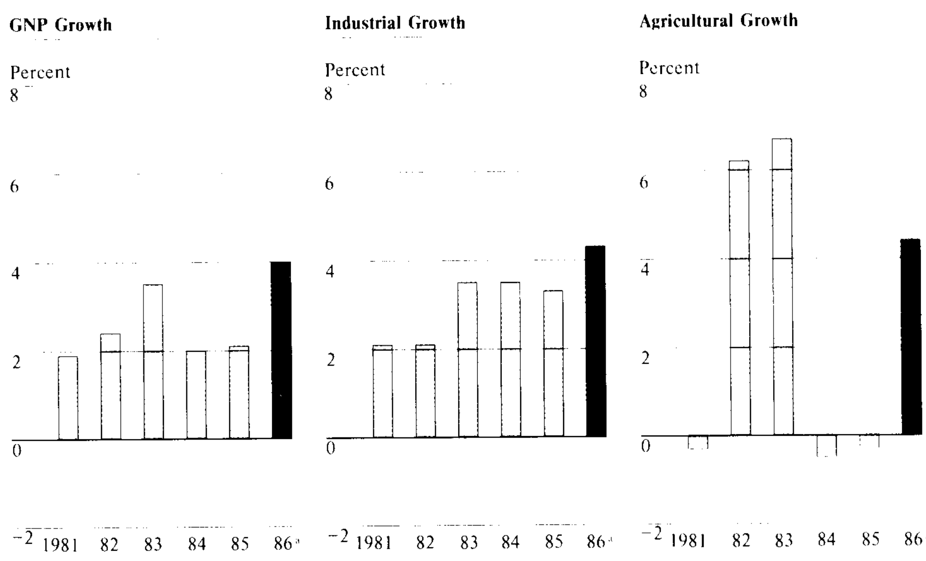
The dismissal last week of internationally respected economist, Mahbubul Haq, is likely to complicate relations with India and sidetrack efforts at economic reform. Haq, the key architect of improved trade ties to India and a proponent of increased deregulation of Pakistan's economy, was replaced by Yasin Kahn Watto, a seasoned politician but a novice in economic affairs. According to press reports [redacted] Haq was fired because he 25X1 moved too fast in improving trade ties to India, supported unpopular economic reform, and was not the "approachable" minister the new civilian government wanted. Because few in the government share Haq's views, improved economic ties to India and US efforts to include economic reforms as a precondition for the new multiyear aid package (FY 1988-93) may well be undermined. [redacted] 25X1

Communist

Soviet Economic Growth in 1985

Disappointing farm output held GNP growth to about 2 percent, but General Secretary Gorbachev can claim some credit for a recovery in growth in the nonagricultural economy after the poor first quarter. Agricultural output shrank for the second year in a row, although an improved grain harvest allowed Moscow to cut grain imports substantially. Industrial production rose by over 3 percent in 1985, slightly below the 3.5-percent pace in 1983 and 1984 but averaging nearly 4 percent during the last three quarters. Growth in energy production slowed. A drop of nearly 3 percent in oil production dampened the effect of a 9-percent increase in natural gas and smaller increases in coal and electricity. The worst winter in two decades cut power supplies, caused numerous equipment breakdowns, and delayed deliveries of raw materials and finished products. Per capita consumption grew more slowly than in 1984, in part because of stagnation in the availability of foods. Growth in investment was about 3 percent, faster than the previous year but not as high as in the early 1980s. The recovery of industrial materials production, aided by increased rail capacity, probably will help growth in 1986, although Soviet goals are ambitious—about 4 percent for GNP, nearly 4.5 percent for industry, and more than 6.5 percent for machine building. 25X1

Soviet Economic Performance, 1981-86



[a] Planned.

25X1

308079 2 86

Strains in Cuban-Soviet Economic Ties

Cuba's economic outlook for the next few years is clouded by increasing Soviet criticism of Cuban inefficiency, and Moscow's unwillingness to increase oil deliveries or economic assistance beyond current levels for 1986-90. Talks last October on economic aid for Havana's 1986-90 plan were strained and no aid agreement was reached, according to a former Cuban official. [redacted] 25X1

Moscow has probably decided to use the new Cuban plan to negotiate a more equitable arrangement. Probably as a result, Cuba's draft economic plan, to be approved in early February, emphasizes increased use of market mechanisms such as profits and incentives. [redacted] 25X1

New Soviet Commission on Economic Reform

A Western diplomat, citing a reliable Soviet source, has told the US Embassy in Moscow that state planning chief Nikolay Talyzin has been named to head the commission on management and planning reform recently established within the government. The new commission will replace a Politburo commission that had been headed by former Premier Tikhonov. The designation of Talyzin to head the new commission suggests that work on economic reform will be concentrated within the State Planning Committee, where several other groups have been studying ways to improve Soviet planning and management. Such a move would reduce the friction among separate and often competing agencies charged with developing reform proposals. That the commission is only now being set up suggests that Soviet leaders are still nowhere near reaching agreement on a comprehensive economic reform program. [redacted] 25X1

China Posts Record 1985 Trade Deficit

According to the Ministry of Foreign Economic Relations and Trade, China last year posted a record $7.6 billion trade deficit—a fivefold increase over the reported 1984 deficit. Chinese customs statistics, which closely correspond with our estimates, indicate an even higher yearend deficit of $10.6 billion. The customs data show that exports grew only 2 percent in 1985, with sharply lower sales of cotton cloth, textiles, and apparel, while imports—primarily industrial raw materials and consumer durables—skyrocketed by 45 percent. Despite the record deficit, Beijing has announced no new measures to narrow the gap. Tighter credit and import restrictions introduced early last year will probably continue, but these efforts will be insufficient to alter China's trade balance significantly in the near term. [redacted] 25X1

Declassified in Part - Sanitized Copy Approved for Release 2011/12/08 : CIA-RDP88-00798R000300020005-4

Page Denied