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24 April 1986

MEMORANDUM FOR: Director of Central Intelligence
Deputy Director of Central Intelligence

FROM: SA/DCI

SUBJECT: Meeting with Acting Deputy Secretary of State and
Director, INR

1. You are scheduled to meet with Acting Deputy Secretary Armacost and D/INR Abramowitz at 1215 on 25 April 1986 at the State Department.

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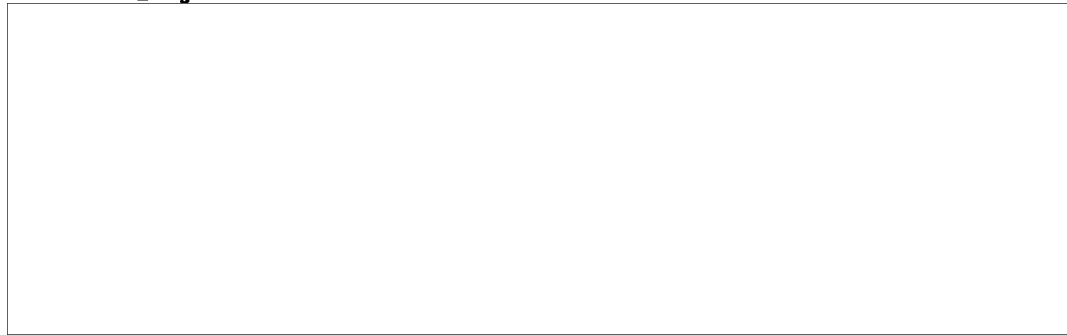
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TAB B Internal Situation in Libya. This TAB contains talking points from DI/NESA re the above subject. The situation in Libya appears to be returning to normal, even though Qadhafi's low profile suggests he continues to concentrate on internal matters. The bleak economic outlook and signs of growing West European solidarity with the U.S. with regard to Libya will complicate the government's ability to focus attention on the U.S. threat and rally popular support.

TAB C Syrian/Libyan Cooperation. This TAB contains talking points from DI/NESA re the level of Syrian support to Libya in the aftermath of the U.S. air strikes.

- Syria is the only Arab state actively providing support for Tripoli and has sent fighter pilots and air defense technicians in recent weeks.
- Syria appears to have been a silent partner in at least the most recent terrorist actions supported/directed by Libya.



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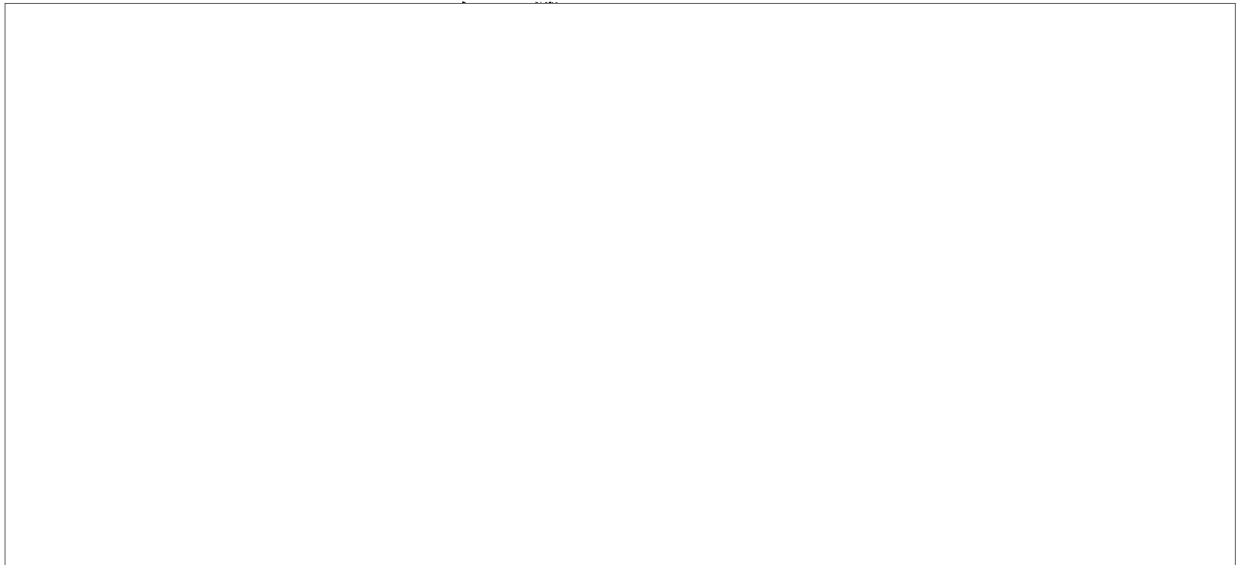


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TAB F

Mexican Economy. Attached are talking points from Acting NIO/Econ on the Mexican financial situation. State indicated an interest in reviewing this subject. In addition to the talking points, I have included:

-- A 29 March special analysis from the NID;

-- A memo of 27 February from [redacted] re implications of Mexico's financial problems;

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This material is provided to you for background inasmuch as State was not explicit as to what specifically they wish to discuss re the Mexican economic situation.

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Talking Points for the DCI

24 April 1986

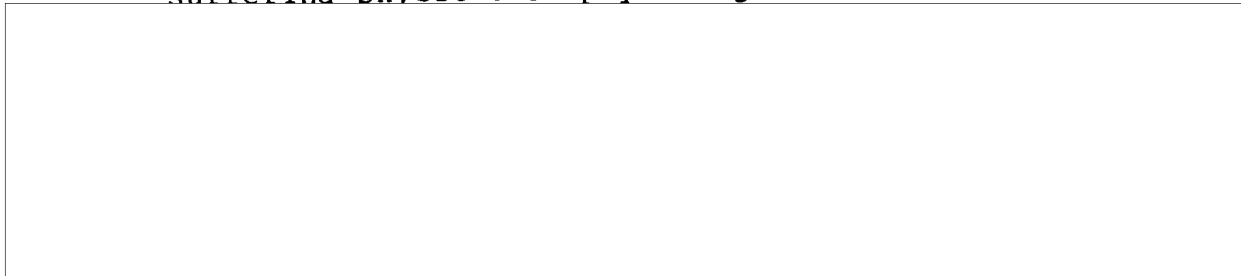
The Internal Situation in Libya

The situation in Libya appears to be returning to normal, even though Qadhafi's low profile suggests he continues to concentrate on internal matters. The bleak economic outlook and signs of growing West European solidarity with the US with regard to Libya will complicate the government's ability to focus attention on the US threat and rally popular support.



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- Qadhafi continues to meet with foreign leaders and delegations, although he has kept public appearances to a minimum. There is little evidence that Qadhafi is suffering physical or psychological distress.



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Uncertainty within the regime also is reflected in its treatment of foreign journalists and diplomats.

- The government vacillated in following through on its announcement to a gathering of about 300 foreign journalists yesterday that they must leave the country immediately.

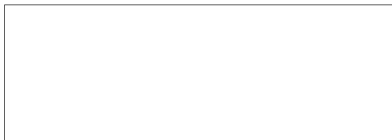


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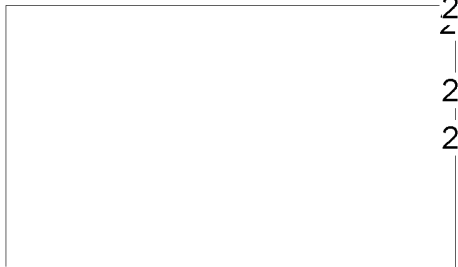
- Although the government has threatened to retaliate for new restrictions on resident Libyans by EC governments, it would not want to take actions which support Washington's diplomatic efforts in Western Europe to undercut Tripoli.



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25X1Economic Update

US sanctions so far have had a varying impact on the Libyan economy.

- The freeze on Libyan financial assets has had the greatest impact. Libya lost access to as much as \$800 million of its \$6.0 billion in foreign exchange reserves. Remaining liquid reserves are sufficient to cover 6 months of imports.
- We estimate that Libya has boosted its crude oil exports to 1.2 million barrels per day, slightly above the level current in early January 1986. Domestic oil workers and foreign workers probably can maintain production or even increase oil production.
- Qadhafi has taken no significant action against US or British workers in response to US air strikes and has attempted to dispell latent fears in the foreign community to retain their badly needed expertise. US service companies and most US technicians reportedly are being replaced by firms and personnel from the United Kingdom, Canada, France, and West Germany.
- [redacted] food lines are growing longer and more contentious as people search for basic staples. Hoarding has become a way of life for most and a thriving black market has evolved, despite government efforts to suppress such activity. 25X1
- The quality of health care and education, hallmarks of Qadhafi's revolution, has fallen off sharply leading most Libyans to agree that Qadhafi's economic policies are a failure. Radical changes in university curriculums have recently resulted in student unrest at some campuses.
- The regime has consolidated its control over the economy by reducing by half the number of government ministries--including the Petroleum Ministry--and transferring these duties to loyal, though less competent managers. 25X1

Soft oil market conditions pose the greatest threat to the economy and probably the regime. Tripoli loses \$440 million annually for each one dollar decline in oil prices at current export levels. Conversely, every 100,000-b/d drop in oil exports cost the regime \$730 million at a \$20 per barrel price.

- An average price of \$15 per barrel would force Tripoli to make difficult and risky political choices. Necessary cuts in imports almost certainly would hit both civilian consumer goods and military equipment as

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[REDACTED]

well as priority projects. Unconfirmed reports say the regime may cut imports by half to conserve foreign exchange.

- Declining oil revenues will hinder Tripoli's ability to repay some \$4 billion in arrears owed to major trade partners in Western Europe and to maintain Libya's oil-for-arms barter arrangement with the USSR. [REDACTED]

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Talking Points for the DCI

23 April 1986

Syria-Libya: Cooperation Following US Airstrikes

Syria has offered Tripoli military assistance following the US attack, but its diplomatic efforts on Libya's behalf have been minimal. There are no indications that the attack has disrupted normal US diplomatic relations with the Syrian regime, nor have the Syrians been prepared to actively back Libyan demands that an Arab Summit be convened to address the US action.

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[Redacted]

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Expanded Military Assistance

Since the US airstrikes against Libya, Damascus has quietly provided military assistance, but little diplomatic support, to Tripoli. Syria's recent commitment of technically-skilled personnel to Libya suggests closer solidarity between the two countries than previously existed.

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Syria is the only Arab state providing active support for Tripoli and reportedly has sent an undetermined number of fighter pilots and air defense technicians in recent weeks.

- The Syrian military probably could ill-afford losing skilled personnel at this time: it has been on heightened alert since late March, probably fearing an Israeli attack, but also possibly due to uncertainty about US retaliatory actions in the event Damascus was linked with terrorist incidents.

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Syria's donation of valuable, trained personnel underscores its concern about the failure of Libyan air defense systems-- which are similar to Syria's--to counter US airstrikes. Damascus is particularly concerned that Israel may obtain sensitive information from the United States on the systems' capabilities.

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[Redacted]

Whatever their numbers, we believe Syrian pilots and technicians in Libya will take a more active role in training Libyans and may become directly involved in any future clashes with US forces.

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[Redacted]

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Terrorism

We do not have conclusive evidence of terrorist cooperation between Syria and Libya. [Redacted]

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[Redacted] Syria is a major practitioner and patron of terrorism [Redacted]

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[Redacted]

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[Redacted]

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Syrian President Assad is on record vowing retaliation for Israel's interception of a Libyan jet on 4 February which was carrying Syrian Ba'th Party officials.

- At the time Assad indicated Syrian revenge would not be directed at civilian targets which, he said, would make Syrians no better than the Israelis whom he accused of air piracy and international terrorism. [Redacted]

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Syria uses terrorism to maintain Syrian dominance in Lebanon, thwart movement toward peace negotiations between moderate Arabs and Israel, extract financial support from certain Arab states in the form of "protection money," and eliminate Syrian dissidents.

- Syria has never been directly implicated in acts of gratuitous violence against non-Arab civilians in Europe.

- Syrian complicity in the El Al bombing would suggest a shift in its guidelines for the use of terrorism or that its extensive security apparatus is running amok. [Redacted]

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The Director of Central Intelligence
Washington, D.C. 20505

National Intelligence Council

NIC 02067-86
23 April 1986

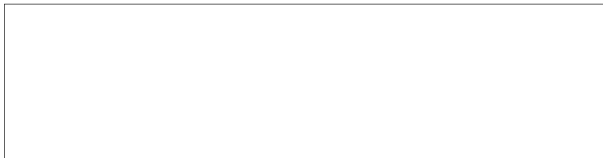
MEMORANDUM FOR: Director of Central Intelligence
Deputy Director of Central Intelligence

THROUGH: Acting Chairman, National Intelligence Council

FROM: Acting National Intelligence Officer for Economics

SUBJECT: Background Material for DCI Meeting with Admiral
Poindexter

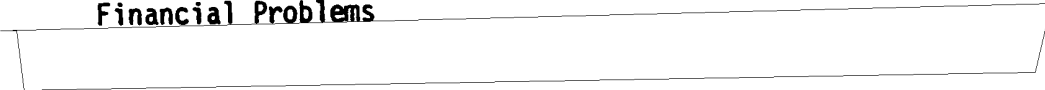
Attached are talking points on the Mexican financial situation for your Thursday meeting with Admiral Poindexter. Among the attachments are an update of the financial situation and a note I sent to you in late February suggesting that the NSC review the Mexican situation.



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Attachments:

1. Talking Points
2. Update on the Mexican Financial Situation
3. 29 March 86 NID: "Mexico: Problems Likely in Debt Negotiations"
4. 27 February Memorandum to the DCI: Implications of Mexico's Financial Problems



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23 April 1936

Mexican SituationTalking Points

The Mexican financial situation is unfolding about as we had anticipated.

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- In discussions with the U.S. Treasury, Mexico has indicated that it will need only \$4 billion in "new money" this year, but internal working documents show a need for \$6.5 billion even using some optimistic assumptions about trade and capital flight.
- Even with an infusion of funds, the economy will contract this year, with per capita income declining by 5 percent or more.
- The budget is under severe pressure from lower oil prices--the average price for Mexico was \$11 per barrel in March, and oil export volume this year has been running 20 to 40 percent below normal levels.

Mexico has been able to stay current on its foreign interest payments, perhaps because tight domestic credit is forcing some firms to repatriate capital to meet expenses.

I think that any decision on helping Mexico out financially should encompass issues beyond economic reform.

- Financial concessions granted to Mexico will spill over into other Latin countries, most of which have done more to improve their domestic conditions than Mexico.
- The full cabinet should decide what price Mexico should pay for a bailout, including policy toward Nicaragua, drug issues, economic reform, etc. If we target everything, past experience shows we will get nothing.

We might also want to consider whether the best way to get long-term economic reform is to tell Mexico to work out its problems with private creditors.

- Such an action would entail some short-term costs to the Mexican economy and the political relationship.
- It might, however, offer the best prospect for spurring long-term economic reform.
- It would also show other creditors such as Brazil and Argentina that we will be willing to help them only if they help themselves.

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23 April 1986

Update on the Mexican Financial Situation

Mexico, the US Government, and the IMF are still discussing Mexico's financial "needs" for 1986.

- Mexico estimates it needs around \$6.5 billion in "new" money including \$3.5 billion from commercial banks, \$2 billion in bilateral credits, and \$1 billion in multilateral assistance. The estimate assumes the roughly \$4 billion in principal due this year will be postponed.
- Treasury and the IMF are holding out for an austerity package, including limits on the government deficit and structural changes aimed at reducing the role of government.
- Treasury wants the World Bank to monitor compliance and to disburse Bank lending in increments pegged to performance. Treasury also would like to get commercial banks to link their disbursements to the World Bank increments.

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The government is now projecting a 4 percent decline in GNP this year, even assuming it obtains new funds. Hence, an optimistic assessment is for a 5 to 10 percent decline in per capita income, with a much larger decline should the peso fall sharply absent a substantial infusion of foreign funds.

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The Director of Central Intelligence
Washington, D.C. 20505

National Intelligence Council

NIC #01000-86
27 February 1986

MEMORANDUM FOR: Director of Central Intelligence
Deputy Director of Central Intelligence

VIA: Harold P. Ford
Vice Chairman, National Intelligence Council

FROM:
Acting National Intelligence Officer for Economics

SUBJECT: Implications of Mexico's Financial Problems



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1. I believe a decision to deal with Mexico's financial problems is properly a national security issue and should be discussed before the full Cabinet at an early NSC meeting. My concern is that if Treasury alone has the action, domestic financial equities and wishful thinking on the degree of US leverage will result in a decision that, in effect, perpetuates the status quo. The decision as to how to proceed with Mexico is one of substantial importance to various entities of the USG additional to Treasury.

- Any bailout will spill over into other Latin countries, some of which (Ecuador, Chile, Argentina) will argue--correctly--that they have done more to get their domestic houses in order than has Mexico.
- Secondly, the full Cabinet should decide what specific price Mexico should pay for a bailout: whether primarily Nicaragua policy, drug traffic, economic reform, etc. (Past experience indicates that if we target all, or too generally, we get none.)
- Lastly, the Cabinet should discuss the option of offering no bailout, singling out Mexico among the major debtors as having behaved particularly poorly.

2. In my view, a strong argument can be made that we should cut the Mexicans off.

- Clearly, the post-1982 bailout has given us no leverage over Mexico concerning Central American policy, drug traffic, or economic reform.

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- Worse, the bailout conditioned the Mexicans to believe that we so feared the effects of a default that we would put up funds in exchange for hollow promises.

3. I believe that if we tell Mexico City to deal directly with its private creditors and continue our efforts to work with countries such as Argentina and Ecuador, we would reinforce proper economic adjustment programs. Furthermore, such an action would send a message to countries such as Brazil that we do not stand ready to pay for populist economic programs.

- A cutoff of Mexico would also help set the stage for the PRI to consider its political future given the realities of oil prices, Mexican oil reserves, and the prospect for not getting several billion dollars in new loans which, in effect, amounts to campaign financing.

4. A major risk, of course, is that a cutoff may strengthen the more radical, leftist elements in the ruling party who will want to put all the blame on the US and who would oppose any reforms that favor free enterprise.

- The US would also suffer from a substantial increase in illegal immigration.
- Other debtors could see the US is inflexible, although I believe this can be handled if we treat each individually and on the basis of merit rather than domestic financial exigencies.

5. At a minimum, I think we should take the time to debate these issues, gauge to what extent the risks may only be short-term and whether on balance the bilateral relationship and Mexico itself would benefit in the long run.

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The Director of Central Intelligence

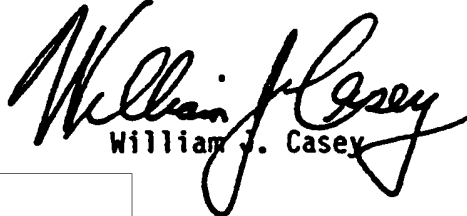
Washington D C 20505

26 February 1986

MEMORANDUM FOR: VADM John M. Poindexter
Assistant to the President for National
Security Affairs

SUBJECT: Mexican Financial Problems

The attached Estimate on implications of Mexico's financial and economic difficulties paints a bleak picture indeed. Even a substantial financial bailout by the international community is only likely to buy the Mexican government more time. Without a decision by the PRI to undertake massive economic reform, which is unlikely, I fear the political situation in Mexico will deteriorate badly over the next 2 to 3 years with major implications for a wide variety of US concerns ranging from narcotics traffic, to illegal migration, to the very stability of the Mexican government itself. Furthermore, if other LDC debtors come to feel that Mexico is getting a bailout with little genuine reform or, for that matter, is able to take unilateral action without apparent serious penalty, some will likely attempt to follow suit.


William J. Casey

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