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Current Intelligence Weekly Summary

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National Foreign Assessment Center

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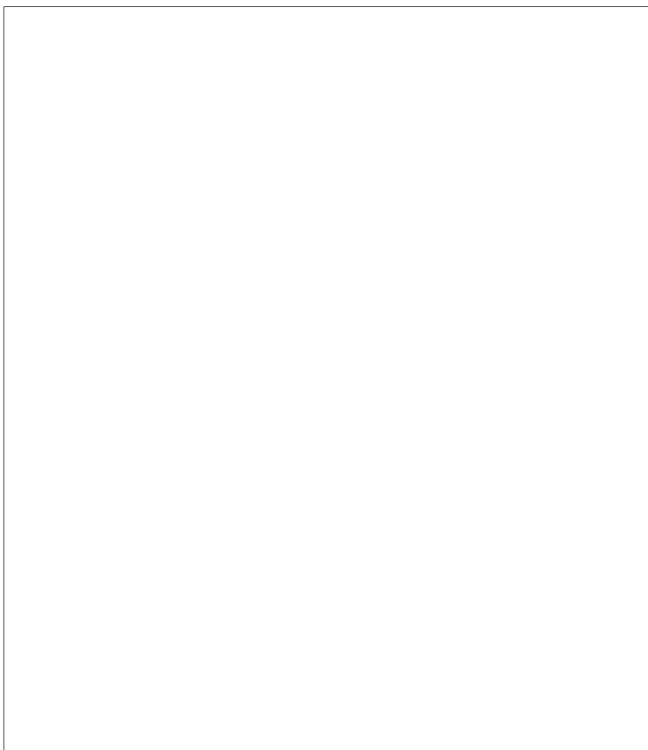
30 June 1978

The WEEKLY SUMMARY, issued every Friday morning by the Current Reporting Group, reports and analyzes significant developments of the week through noon on Thursday. It frequently includes material coordinated with or prepared by the Office of Regional and Political Analysis, the Office of Economic Research, the Office of Strategic Research, the Office of Scientific Intelligence, the Office of Weapons Intelligence, and the Office of Geographic and Cartographic Research.

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13 *Argentina: Economic Outlook*

Comments and queries on the contents of this publication are welcome. They may be directed to the editor of the Weekly, telephone:

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Argentina: Economic Outlook

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The economic strategy of the Argentine military government is faltering, and the country may fall back into the pattern of fluctuating economic policies that has plagued it since the 1930s. Economic stagnation and lack of progress in the anti-inflation drive have weakened the position of Minister of Economy Martinez de Hoz, who has been instrumental in implementing the military junta's economic reform program.

The junta, which overturned the Peron government in March 1976, faced economic and financial problems unparalleled in Argentina's history. The economy was

in chaos, with foreign exchange reserves practically exhausted and the country on the verge of defaulting on its foreign debt. Soaring wages and a swollen government deficit had pushed inflation close to a 750-percent annual rate. Import restrictions and sporadic price controls had induced a steep decline in production.

The junta instituted an economic reform program that touched nearly every aspect of the economy: most price controls were lifted; wages were controlled and activities of labor unions sharply curtailed; the government's involvement in the economy was reduced; trade restrictions were eased; and controls over interest rates were removed. Loans totaling \$1 billion

from the International Monetary Fund and commercial banks helped to restructure the foreign debt, and good weather and agricultural incentives yielded a bumper export crop to make economic prospects even brighter.

By the end of 1977, 21 months after assuming power, the junta had:

- Achieved a trade surplus half again as large as the \$1 billion deficit it inherited.
- Raised reserves to a level equal to a year's imports.
- Sharply cut the budget deficit.
- Lowered the 12-month inflation rate to 175 percent.

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- Reversed two years of decline in gross domestic product—which grew by 4.4 percent in 1977.

The recovery, however, was fragile because it was based on a bumper year for agricultural exports and a spurt in investment spending. At the end of 1977, real incomes and purchasing power were still below the 1975 level.

A Blow to the Recovery Program

The economy performed dismally in the first quarter of 1978. National output, registering its first quarterly drop since mid-1976, declined by 7.2 percent compared with the first quarter in 1977. Production fell off in all sectors except construction. Agriculture—plagued by unfavorable weather and low world wheat prices—was down 7 percent. Manufacturing—hobbled by the public's continuing low purchasing power and lower demand from the farm sector—fell 11.5 percent.

Despite the drop in production, the government has failed to make headway in contolling triple-digit inflation—its top priority in 1978. The consumer price index increased by a discouraging 46 percent in the first four months, above last year's 41 percent for the same period. The inflationary spurt was attributable largely to a rapid rise in the money supply, increased public utility rates, and inflationary expectations in the private sector that contributed to price rises.

Government Reaction

The government responded quickly once the first quarter results were in. To counter inflation, import tariffs on products that have experienced sharp price rises will be reduced and government operations in the foreign exchange market to control "minidevaluations" of the peso will be halted. In addition, local currency deposits will be required against foreign loans to minimize the impact of foreign capital inflows on the money supply.

To counter the recession, the government plans to increase the purchasing

power of farmers, small businessmen, and households with credit on more favorable terms, to lower bank reserve requirements, to facilitate the importation of industrial materials and equipment, and to keep tariffs at a minimum. Special legislation is being prepared to stimulate Argentina's important automotive industry, which has been especially hard hit by the recession.

Prospects

The economy probably will begin to pick up by the end of the second quarter or early in the third; the new economic measures should slow the recession and the inflation rate. An unexpectedly good harvest of coarse grains will improve agriculture's performance for the year and help to sustain farmers' purchasing power. The recent World Cup soccer matches attracted many visitors and stimulated

spending, although less than the event's planners had expected.

Economic growth for the year, however, will likely be less than 1 percent and may even be negative. Moreover, the high inflation rate of the first four months will make it difficult for the government to hold annual inflation below 150 percent, much less reach the official two-digit goal.

During the past several months, opposition to Martinez de Hoz and his policies has been widespread, especially among workers and small businessmen caught in the stagflation squeeze. Even highly placed officials—among them junta member Admiral Massera—have openly criticized the Minister. For the time being, however, he continues to enjoy the support of President Videla and most of the Army, the most influential of the armed services.

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Happy soccer crowds in Buenos Aires

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