277-0613
NE/PD Files
FY79
277-K-104

UNCLASSIFIED

PD-AAM-463

(2)

DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
Washington, D. C. 20523

Proposal and Recommendations
For the Review of the
Near East Advisory Committee

TURKEY - PROGRAM ASSISTANCE

AID Loan No. 277-K-104

UNCLASSIFIED

TURKEY
PROGRAM ASSISTANCE PAPER

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Program Assistance Approval Document (PAAD)

CLASSIFICATION: UNCLASSIFIED

AID 1120-1 (8-68)

PAAD

DEPARTMENT OF STATE
AGENCY FOR
INTERNATIONAL DEVELOPMENT

PROGRAM ASSISTANCE
APPROVAL DOCUMENT

1. PAAD NO. NE 79-1 (AID Loan No. 277-K-104)

2. COUNTRY Turkey

3. CATEGORY Cash Transfer

4. DATE October 20, 1978

5. OYB CHANGE NO.

6. TO: The Deputy Administrator

7. FROM: AA/NE, Joseph C. Wheeler

8. OYB INCREASE

TO BE TAKEN FROM:

9. APPROVAL REQUESTED FOR COMMITMENT OF: $50,000,000

10. APPROPRIATION – ALLOTMENT: 72-1191037 937-62-298-00-58-91

11. TYPE FUNDING: [X] LOAN [ ] GRANT

12. LOCAL CURRENCY ARRANGEMENT: [ ] INFORMAL [ ] FORMAL [X] NONE

13. ESTIMATED DELIVERY PERIOD: Not Applicable

14. TRANSACTION ELIGIBILITY DATE: Not Applicable

15. COMMODITIES FINANCED

Not Applicable

16. PERMITTED SOURCE		17. ESTIMATED SOURCE	
U.S. only:		U.S.:	Not Applicable
Limited F.W.:		Industrialized Countries:	Not Applicable
Free World:		Local:	Not Applicable
Cash:	$50,000,000	Other:	Not Applicable

18. SUMMARY DESCRIPTION

Authorization is requested for a $50 million balance of payments cash loan to Turkey designed to alleviate Turkey's foreign exchange shortage.

Turkey is struggling with severe balance of payments problems brought about by a combination of internal and external factors, including the policies of previous governments to sustain rapid economic growth through an investment program that relied heavily on imports of capital and intermediate goods, the economic slowdown in western Europe which adversely affected Turkish export earnings and remittances by Turkish workers, and increased oil prices. The deficit on its current account reached $3.4 billion in 1977; a $2.0 billion deficit is projected for 1978.

The present Government has taken a series of measures to bring the economy under control. A comprehensive package of stabilization measures was formulated which

19. Clearances	Date
NE/PD:SATaubenblatt	11/8/78
NE/NENA:JKnoll	11/3/78
NE/DP:BLangmaid	11/4/78
EUR/SE:AHFlanigan/RCEwing	11/6/78
EB/IFD/OMA:MECEly	11/7/78
TREAS:JBlainey(Subs)	10/27/78
GC/NE:JMiller	11/15/78
GC:MBall	11/15/78
FM:MDStafford	11/13/78
PPC/DPRE:EBHogan	11/16/78
AA/PPC:AShakow	11/17/78
AA/NE:ADWhite	11/14/78

20. ACTION

[X] APPROVED [ ] DISAPPROVED

AUTHORIZED SIGNATURE — DATE 11/24/78

TITLE

formed the basis for a Standby Agreement with the IMF in April 1978. But stabilization of the economy will inevitably take some time, especially if intolerable dislocation of the domestic economy is to be avoided. Turkey is therefore seeking support from her western allies. The FRG, Norway, France and Austria are providing loans, and a 14 nation debt rescheduling, including the USG, has been negotiated.

The outcome of Turkey's efforts to overcome the problems of the economy is of considerable interest to the U.S. Turkey is a NATO ally, is situated in a complex area in which the U.S. has important interests, and is a large nation facing the challenge of development in a democratic political framework. The proposed loan - which will be disbursed as a cash transfer - will have an immediate impact in helping Turkey meet its international payment obligations as well as provide a concrete demonstration of our concern for the economic problems of an ally. A commodity import program can neither achieve the quick-disbursing balance of payments support Turkey needs nor is feasible under present conditions. It is expected that the funds will be disbursed within one month of the signing of the loan agreement. Overall, this loan is consistent with the objectives of the FY 1979 Economic Support Fund legislation.

The loan will provide for a ten-year maturity, including a grace period of three years. Interest will be at the approximate cost of ten-year money to the U.S. Treasury (currently about 8.75 to 9 percent per annum)

Recommendations:

It is recommended that you authorize a cash transfer loan to Turkey of $50,000,000 from funds appropriated under the Economic Support Fund account of the Foreign Assistance Act of 1961, as amended, for balance of payments assistance on the following terms:

1. Borrower shall repay the loan to A.I.D. in U.S. dollars within ten (10) years from the date of the disbursement under the loan, including a grace period of three (3) years. Borrower shall pay interest at a rate to be fixed by the U.S. Department of Treasury on the date that loan negotiations with the Borrower commence, said rate to be based on the cost as of that date of ten-year money to the U.S. Treasury.

2. In addition to the standard requirements of a legal opinion from Borrower and appointment of representatives, the loan shall be subject to such other terms and conditions as A.I.D. may deem advisable.

Attachments:

1. Supporting Analysis
2. Statutory Checklist
3. Draft Loan Agreement

<u>Program Assistance Committee</u>

G. Evans, NE/PD Chairperson
E.J. Marcott, EUR/SE
N. Tumavick, NE/NENA
J. Miller, GC/NE
R. B. Perry, NE/PD

Supporting Analysis

I. Political and Economic Considerations

The relationship between the U.S. and Turkey has several significant facets. Turkey is a NATO ally, is situated in a complex area in which the U.S. has important interests, and is a large nation facing the challenge of development in a democratic political framework. Since the early days of its republic, Turkey has looked to the West for its primary political, economic and cultural relationships.

Strengthening the bilateral relationship with Turkey is a vital and fundamental goal of United States policy in the eastern Mediterranean region. Common security concerns of both countries are an important element of this evolving relationship. As part of a program for revitalizing the U.S./Turkish relationship, the arms embargo enacted in 1975 in response to Turkish action on Cyprus in 1974, was repealed so that the U.S. could more fully cooperate with Turkey in a manner consonant with the requirements of an alliance important to the mutual security of both countries.

The $50,000,000 loan proposed herein is also a critical component of the Administration's comprehensive program for strengthening ties with Turkey. Turkey is presently undergoing serious economic problems, and the loan will assist Turkish efforts to stabilize the economic situation as well as provide a concrete indication of United States concern for Turkey's economic problems.

The U.S. Congress, responding to a supplemental budget request for $50,000,000 to provide the Government of Turkey with immediately available foreign exchange resources to meet short-term balance of payments requirements, has authorized and appropriated $50,000,000 under the Economic Support Fund account of the Foreign Assistance Act for the purposes requested.

II. Economic Overview

In most respects, the record of Turkish economic developments over the last two decades has been poor. While economic growth in real terms averaged 7.3% since 1970, about 4.8% per capita, which is indeed commendable, it was accompanied by high inflation and unemployment and an overvalued exchange rate which led to critical balance of payments problems. These developments reflect government policies to force industrial growth aimed at import substitution through the development of relatively capital intensive government owned industries heavily dependent upon budget support as a result of unrealistic pricing policies and inefficiency. These expenditures brought large budget deficits financed by Central Bank expansion of the money supply. Unfortunately, this situation was aggravated by a general recession in Europe which curtailed demand for Turkey's exports and greatly reduced the inflow of workers' remittances upon which Turkey was so heavily dependent. As a result, the GOT became increasingly dependent upon foreign credits and the additional pressure of debt servicing helped bring a crisis which required debt rescheduling in May 1978 and an IMF standby at about the same time.

The emphasis which successive governments have laid on industrialization has been reflected in a doubling of the share of the industrial sector in total output between 1955 and 1977. It has also resulted in comparative neglect of agricultural development, which has in addition been hampered by inappropriate subsidy and pricing policies. Moreover, a strong emphasis on sophisticated capital-intensive technology has resulted in high-cost production in certain sectors; and protection against competition from imports has inhibited the development of a sound industrial structure well-suited to Turkey's comparative advantages in terms of location, natural resources and labor availability. One important consequence of this, in the context of a foreign trade strategy which has emphasized import-substitution, has been that Turkey has so far been unable to develop a strong industrial export base, and has relied mainly instead on its traditional agricultural exports (supplemented by workers' remittances) to finance the imports of materials and capital goods needed for its ambitious modernization effort. This pattern of trade has been a fundamental cause of the difficulty which Turkey has periodically experienced in reconciling rapid growth with a viable external payments position.

The year 1977 was extremely difficult and strained for the Turkish economy. The payments problems caused may foreign suppliers to restrict or terminate deliveries to Turkey, as debts owed to them rose. Since the Turkish economy is dependent upon imported raw materials, capital equipment and intermediate goods, unemployment rose rapidly, reaching an estimated 13.5 percent in 1977, and shortages contributed to traditionally high inflation, driving it up to an estimated 25 percent on an annual basis by the end of the year. Nothwithstanding the restrictions by foreign suppliers, the current account deficit reached $3.4 billion in 1977 (oil imports totaled some $1.8 billion) as exrort receipts and remittances by Turkish workers failed to grow in proportion to imports.

The substantial current account deficits of 1975-1977 were initially financed through a drawdown of reserves and by short-term borrowing in the Euromarkets which eventually totalled nearly $2 billion. By early 1977, this source of foreign capital had been exhausted, and the Central Bank was unable to effect transfer of foreign exchange for all but the most vital imports and some debt service payments. By the end of 1977, Turkey's short term external debt position stood at $5.4 billicn.

In September 1977 the government initiated negotiations with the IMF. After a change in government in January 1978, a comprehensive package of stabilization measures was formulated which formed the basis for a Standby Agreement signed on April 24, 1978.

The Turkish government has taken a number of measures to bring the economy under control. To discourage imports, and stimulate exports, the lira has been devalued against the dollar three times since September 1977 by a total of about 30 percent. In addition, it has drifted downwards with the dollar against other currencies. The 1978 budget contained reductions, in real terms, in expenditures and in the deficit from 1977. Substantial price increases for the products of state economic enterprises (air, railroad and shipping tariffs, electricity tariffs, and the prices of coal, iron and steel products and petrochemicals) are expected to increase revenues by about TL 25 billion (equivalent to 3 percent of 1977 GDP) in a full year. The government has also established and consolidated several schemes for giving companies priority access to foreign exchange for imports needed to maintain export promotion. Essentially, these schemes accelerate and assure positive action of exporters' requests for foreign exchange needed to buy imports for production. Procedures for Eurodollar borrowing have been revised to deter its use in financing specific transactions and to bring it more under Central Bank control. The projections for 1978 nonetheless point to a current deficit of $2.0 billion (from $3.4 billion in 1977), the reduction largely being the result of a shortage of import financing rather than improved export performance.

These efforts will help toward alleviating Turkey's economic difficulties, but during the coming months the situation could deteriorate further. Unemployment has already risen further to 20%, possibly reflecting some pressures for structural changes in the economy moving away from import substitution. Moreover, largely as a result of more costly imports and rising prices of products of state enterprises, inflation reached an annual rate of 70% by September 1978. These events probably more than offset the end of 1977 wage increase and are likely to bring pressures for renewed demands by labor. They may also bring further need for another exchange rate depreciation. The question of whether the GOT can continue this difficult program is thus heavily dependent upon internal support of its policies.

Foreign exchange reserves are very low. Even with optimal external and internal economic policies, there are physical and financial limits to the speed with which exports (especially industrial exports) and workers' remittances can be expanded in the short term, particularly in the present climate of slow trade growth. Thus to maintain essential imports, Turkey must in the immediate future rely heavily on external borrowing to cover projected current account deficits.

III. Balance of Payments

A. General

The most prominent feature of the crisis of 1977 was the large resource gap, which amounted to almost $4 billion, or 9 percent of GDP.

But this did not arise overnight; the resource gap had been widening steadily since 1973, when it was only $0.6 billion, or 3 percent of GDP

One aspect of this marked deterioration in Turkey's external trading position was a very rapid increase in imports, which nearly tripled in value between 1973 and 1977, when they reached $5.8 billion. Approximately half of this increase was due to rising world prices, including a four-fold rise in the price of oil, which currently accounts for about a quarter of the total import bill. The other half of the increase was due to a steep rise in the volume of imports, which grew at about 15 percent per annum, roughly double the growth rate of real GDP.

This high import propensity has been characteristic of Turkey in the 1970s, and may be seen partly as a "catching up" phenomenon. In 1970, after a decade of strict import rationing, the ratio of imports to GDP in Turkey was only 7 percent (about half the average for countries of its size and stage of development). By 1977, after several years of liberalization of import restrictions, this ratio had reached 14 percent, a more typical figure. In concrete terms, however this process was associated with a great increase in the use of imported fertilizer in agriculture, and changes in industrial structure and technology, which increased the dependence of the rapidly growing industrial sector on imported inputs. After 1973, the rate of growth of imports accelerated by a fall in the local currency price of imported goods relative to domestic output due to: a rate of inflation in Turkey which exceeded the international inflation rate by more than the rate of depreciation of the Turkish lira against other currencies; absolute shortages of domestically produced goods; an increase in the share of fixed investment in total expenditure; and possibly also a tendency at times to build up imported stocks in anticipation of devaluation.

B. Current Account Balance

From 1970 to 1973, the rising propensity to import was more or less offset by rapid expansion of exports, particularly manufactured exports such as cotton yarn and fabric, leather products and processed food. In value terms, total exports increased from $588.5 million in 1970 to $1,317 million in 1973, or by 31 percent per annum. Manufactured exports increased even faster—from $100.3 million in 1970 to $443.4 million in 1973, or by 64 percent per annum. In volume terms, total exports during 1970-1973 increased by an average annual rate of 22 percent, a very high rate indeed. Since 1973, however, export performance has been weak. The value of exports rose by 33 percent during 1974 and 1977, when it attained $1.8 billion, mainly due to rising world prices; in volume terms, Turkish exports showed no upward trend. Thus by 1977, merchandise exports were only one-third as large as imports, and the tourism balance was negative.

The poor showing of Turkish exports in 1974-77 is in part attributable to the world recession, but more important, they reflect GOT policies to encourage import substitution and the overvalued exchange rate which held export prices too high. This not only affected industrial exports; it also depressed Turkish agricultural exports such as hazelnuts and raisins and industrial raw materials (cotton and tobacco) Agricultural support prices bore little relation to world prices, and thus failed to provide incentives to farmers to increase production of exportable commodities. This problem was compounded by a general neglect of agricultural development, buoyant domestic demand for agricultural produce, and ineffective administration of agricultural export sales. More importantly, the development of industrial exports, which at present account for only 7 percent of the value of industrial output, was stifled by a more rapid increase of production costs in Turkey then in her trading partners, which was not sufficiently offset by periodic small devaluations of the lira. As a result, and despite considerable increases in tax rebates to exporters, exporting, which had been lucrative for a brief period in the early 1970s, became much less profitable, and potentially exportable production was diverted to the booming and highly profitable domestic market.

The widening resource gap after 1973 was more than fully reflected in the current account balance, which moved from a surplus of $0.5 billion in 1973 to a deficit of $3.4 billion in 1977, because of a decline in workers' remittances from a peak of $1.4 billion in 1974 to around $1 billion in 1977. One important cause of this decline has been the restrictions on immigration imposed by Western European countries in the face of growing domestic unemployment caused by the world recession. But the rate at which foreign earnings were remitted also fell substantially. This was caused in part by changes in the composition of the Turkish emigrant population, including an increase in the proportion of workers allowed to bring their families to join them. In part, it also reflected overvaluation of the lira, which induced migrant workers either to hold their savings abroad or to remit them through unofficial channels.

C. Capital Account

The rapidly rising current account deficit was not matched by an increased inflow of medium and long-term external capital. Turkey has deliberately kept both foreign private investment and private long-term borrowing to a minimum. The gross inflow from official long-term borrowing has stagnated since 1970 at about $350 million per annum. Initially, this was due to a failure to anticipate the need for it, given the tremendous increase in workers' remittances in the early 1970s; subsequently, it was because of a lack of experience and initiative on the part of successive governments to develop and tap new sources of external borrowing when faced with a decline in multilateral and bilateral lending on concessional terms. In 1976 and 1977, long-term loan commitments rose sharply, to over $1 billion per annum. But most of these loans were tied to specific purchases and specific projects, whose implementation has been slow; thus the level of disbursements did not increase. Consequently, the overall balance of payments moved from a surplus of $0.9 billion in 1973 to a deficit of $2.7 billion in 1977. The cumulative deficit from 1974 to 1977 amounted to $6.6 billion. Of this, $1.3 billion was financed by running down the foreign exchange reserves, which by the end of 1977 stood at $770 million, equivalent to only one and a half months' imports. The remainder, amounting to some $5.3 billion, was financed by various forms of short-term borrowing

D. Other Donor Assistance

The IBRD is currently processing a $150 million program assistance loan for high priority imports over the next two years. Under the Standby Agreement, the IMF will be providing approximately $450 million in 1978 and 1979. The Turkish Government has also sought other potential sources of medium and long-term external finance. In response to this initiative, West Germany has agreed to provide program credits of $75 million and project credits of $65 million; France, Norway and Austria have also provided loans; Libya provided a program credit of $100 million, and another $300 million, spread over five years, to finance oil imports; Iran provided a short-term credit of about $135 million for oil imports; trade agreements of about $320 million have been signed with Romania and Bulgaria. Turkey is also negotiating a refinancing of its short-term debt with private banks. Despite these fresh borrowings and rescheduling of debts (discussed below), it is estimated that Turkey will still have a foreign exchange gap in 1978 of approximately $500 million.

The following is a summary of Turkey's balance of payments position.

TURKEY: BALANCE OF PAYMENTS 1/

(In current U.S.$ Millions)

	Actual 1970	Actual 1975	Actual 1976	Actual 1977	Projected 1978
SUMMARY OF BALANCE OF PAYMENTS					
1. Exports and NFS	760	2139	2742	2557	3018
2. Imports and NFS	-1132	-5191	-5735	-6496	-5464
3. Resource Balance	-372	-3052	-2993	-3939	-2446
4. Net Factor Service Income	193	1152	692	549	346
a. Interest (net)	-47	-124	-217	-317	-669
b. Workers' Remittances	273	1312	983	982	1100
c. Profits	-33	-36	-83	-116	-85
5. Transfers (net)	8	20	22	-	60
6. Balance on Current Account	171	-1880	-2301	-3391	-2040
7. Private Direct Investment	59	153	27	67	75
8. Grant and Grantlike Flows 2/	117	98	136	102	100
9. Public M&LT (gross)	337	322	491	310	700
10. Amortization on Public M&LT	-197	-147	119	-214	-242
11. Public M&LT (net)	140	175	372	96	458
12. Short-term Capital (net)	18	840	1451	2713	585
13. IMF (net)	48	197	148	-	200
14. Capital n.i.e. 3/	-24	-	55	413	626
15. Change in Reserves (- = increase)	-186	417	112	546	-4

1/ Totals may not add up because of rounding errors.
2/ Mostly imports with waivers.
3/ Net residual financing and capital not included elsewhere.

Source: IBRD Report No. P-2374-TU dated September 5, 1978

IV. Debt Rescheduling

The extensive short-term borrowing of the past three years greatly increased Turkey's external debt, adversely affected its previously rather attractive foreign debt maturity structure, and caused a sharp rise in debt service payments. At the end of 1977, the country's total external indebtedness amounted to approximately $10.9 billion, of which $0.5 billion was private unguaranteed medium and long-term debt, and $4.2 billion was public or publicly guaranteed medium and long-term debt. Of this, about one-third was held by international organizations and the European Investment Bank; and about one-half by foreign governments and government agencies, notably those of the United States, West Germany, Canada and the Soviet Union. The remaining $6.2 billion of Turkey's total external debt at the end of 1977 consisted of short-term liabilities of various sorts.

In May 1978, thirteen OECD creditor countries and the U.S. agreed on a proposal rescheduling a large portion of Turkey's debt service (on government or government guaranteed debt) that fell due or will fall due between January 1, 1977 and June 30, 1979. Approximately $500 million in short-term debt arrearages are to be rescheduled. Eighty percent of the arrearages will be repaid over a six-year period, including two years grace, while payments on the remaining twenty percent will be made in four semi-annual payments. Representatives also agreed on the rescheduling of arrearages on longer-term debt (i.e. that with a maturity of more than one-year) as well as payments on this debt falling due up through June 30, 1979. The total value of longer term debt is estimated at roughly $600 million, about one-third of which is attributable to the U.S. The following table presents a summary of USG rescheduled debt.

SUMMARY OF USG RESCHEDULED DEBT

(Millions of Dollars)

	Contracts With A Maturity Of More Than One Year	Contracts With A Maturity Of One Year Or Less	TOTAL
Export-Import Bank	55.0	15.0	70.0
P.L.-480	.9	-	.9
Treasury #74002	11.9	-	11.9
Agency for International Development	46.8	-	46.8
Department of Defense	61.3	-	61.3
TOTAL	175.9	15.0	190.9

In 1977, debt service payments, including interest on short-term debt, amounted to 16.7 percent of exports of goods and non-factor services plus workers' remittances. In 1978, after making allowance for the rescheduling of service payments, this ratio is likely to rise to around 25 percent. In subsequent years, it will increase further taking into account new borrowings essential to maintain sound economic growth. In 1982 and 1983, when substantial amortization of consolidated short-term debt is expected to be necessary, the ratio may rise to between 40 and 45 percent. This, however, should represent the culmination of the financial consequences of the present crisis, and thereafter the ratio should decline rapidly, provided the export drive is sustained. Thus, although the balance of payments situation will remain tight in the medium-term future, given sound economic and fiscal policies and careful debt management which the new government shows determination to provide, Turkey continues to have a substantial borrowing capacity for medium and long-terms funds, and remains creditworthy.

In view of the ad hoc nature of the $50,000,000 A.I.D. credit--to assist Turkey's short-term balance of payments-- ten year terms, including a three year grace period, with an interest rate equivalent to the cost of ten year Treasury bonds (about 8.75% to 9%) are proposed.

V. Economic and Repayment Prospects

Turkey's economic situation will be difficult over the next few years. Continued restraint on government expenditures, particularly investment, could affect the expected growth in standard of living and employment levels. The economy will be burdened by its debt service obligation as well as by the costs of the inevitable process of adjustment to a more balanced economy. Prices, particularly of state enterprise products, will continue to rise, albeit less rapidly than in 1977, and the full impact of devaluation on prices will be felt during 1978. Operating in a democratic society, the government will have the difficult task of maintaining austerity in a nation accustomed over the past decade to rapid growth. However, with per capita income around $1000, good geographic location, exploitable natural resources, (though deficient in fossil fuels) and a large labor force, many with experience abroad, Turkey has bright long-term prospects.

Despite the many short-term economic problems discussed above, the actions being taken by Turkey under the IMF Standby, new credits of other donors and potential future economic development and growth in Turkey, make for reasonable prospects for repayment of the A.I.D. $50 million credit.

VI. Loan Adminstration

The schedule for implementation actions leading to the full disbursement of the $50,000,000 credit is as follows:

	Date
Loan Authorization	November 1, 1978
Loan Agreement	November 15, 1978
Conditions Precedent Satisfied	November 20, 1978
Full Disbursement	November 30, 1978

The proceeds of the $50,000,000 loan will be deposited in a U.S. bank designated by the Government of Turkey.

VII. Recommendation

It is recommended that A.I.D. authorize a loan to Turkey of $50,000,000 for balance of payments assistance on the following terms and conditions:

A. Repayment in United States dollars within ten (10) years from the date of the disbursement, (cash transfer), including a grace period of three (3) years.

B. Interest will be at the approximate cost of ten-year money to the U.S. Treasury (approximately 8.75 to 9 percent per annum).

C. The loan shall be subject to such other terms and conditions as A.I.D. may deem advisable.

Copy of the loan agreement is attached as Annex B.

TURKEY FY 1979

COUNTRY CHECKLIST

Listed below are, first, statutory criteria applicable generally to FAA funds, and then criteria applicable to individual fund sources: Development Assistance and Security Supporting Assistance funds.

A. GENERAL CRITERIA FOR COUNTRY

1. FAA Sec. 116. Can it be demonstrated that contemplated assistance will directly benefit the needy? If not, has the Department of State determined that this government has engaged in consistent pattern of gross violations of internationally recognized human rights?

   1. It cannot be so demonstrated; the Department of State has not so determined.

2. FAA Sec. 481. Has it been determined that the government of recipient country has failed to take adequate steps to prevent narcotics drugs and other controlled substances (as defined by the Comprehensive Drug Abuse Prevention and Control Act of 1970) produced or processed, in whole or in part, in such country, or transported through such country, from being sold illegally within the jurisdiction of such country to U.S. Government personnel or their dependents, or from entering the U.S. unlawfully?

   2. It has not been so determined.

3. FAA Sec. 620(b). If assistance is to a government, has the Secretary of State determined that it is not controlled by the international Communist movement?

   3. The Secretary of State has so determined.

4. FAA Sec. 620(c). If assistance is to government, is the government liable as debtor or unconditional guarantor on any debt to a U.S. citizen for goods or services furnished or ordered where (a) such citizen has exhausted available legal remedies and (b) debt is not denied or contested by such government?

   4. Turkey is not known to be in violation of this section.

5. FAA Sec. 620(e) (1). If assistance is to a government, has it (including government agencies or subdivisions) taken any action which has the effect of nationalizing, expropriating, or otherwise seizing ownership or control of property of U.S. citizens or entities beneficially owned by them without taking steps to discharge its obligations toward such citizens or entities?

   5. Turkey is not known to be in violation of this section.

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6. FAA Sec. 620(a), 620(f); App. Sec. 107, 114. Is recipient country a Communist country? Will assistance be provided to the Socialist Republic of Vietnam, Cambodia, Laos, Cuba, Uganda, Mozambique, or Angola?

6. Turkey is not a Communist country. Assistance will not be so provided.

7. FAA Sec. 620(i). Is recipient country in any way involved in (a) subversion of, or military aggression against, the United States or any country receiving U.S. assistance, or (b) the planning of such subversion or aggression?

7. No.

8. FAA Sec. 620(j). Has the country permitted, or failed to take adequate measures to prevent, the damage or destruction, by mob action, of U.S. property?

8. No.

9. FAA Sec. 620(l). If the country has failed to institute the investment guaranty program for the specific risks of expropriation, inconvertibility or confiscation, has the AID Administrator within the past year considered denying assistance to such government for this reason?

9. Turkey has instituted an investment guaranty program (TIAS 2500).

10. FAA Sec. 620(o); Fishermen's Protective Act, Sec. 5. If country has seized, or imposed any penalty or sanction against, any U.S. fishing activities in international waters,

a. has any deduction required by Fishermen's Protective Act been made?

b. has complete denial of assistance been considered by AID Administrator?

10. Turkey has not taken any such actions.

11. FAA Sec. 620(q); App. Sec. 503. (a) Is the government of the recipient country in default on interest or principal of any AID loan to the country? (b) Is country in default exceeding one year on interest or principal on U.S. loan under program for which App. Act appropriates funds, unless debt was earlier disputed, or appropriate steps taken to cure default?

11. No, AID loans and other US loans are presently being rescheduled by U.S. Government.

12. FAA Sec. 620(s). "If contemplated assistance is development loan (including Alliance loan) or security supporting assistance, has the Administrator taken into account the percentage of the country's budget which is for military expenditures, the amount of foreign exchange spent on military equipment and the amount spent for the purchase of sophisticated weapons systems?" (An affirmative answer may refer to the record of the taking into account, e.g.: "Yes as reported in annual report on implementation of Sec. 620(s)." This report is prepared at the time of approval by the Administrator of the Operational Year Budget.

12. Yes, as reported in annual report on implementation of Section 620(s).

A12

Upward changes in the Sec. 620(s) factors occuring in the course of the year, of sufficient significance to indicate that an affirmative answer might need review, should still be reported, but the statutory checklist will not normally be the preferred vehicle to do so.)

13. FAA Sec. 620(t). Has the country severed diplomatic relations with the United States? If so, have they been resumed and have new bilateral assistance agreements been negotiated and entered into since such resumption? — 13. No.

14. FAA Sec. 620(u). What is the payment status of the country's U.N. obligations? If the country is in arrears, were such arrearages taken into account by the AID Administrator in determining the current AID Operational Year Budget? — **14. Turkey is current in its UN obligations.**

15. FAA Sec. 620A. Has the country granted sanctuary from prosecution to any individual or group which has committed an act of international terrorism? — 15. No.

16. FAA Sec. 666. Does the country object, on basis of race, religion, national origin or sex, to the presence of any officer or employee of the U.S. there to carry out economic development program under FAA? — 16. No

17. FAA Sec. 669, 670. *Has the country, after August 3, 1977, delivered or received nuclear enrichment or reprocessing equipment, materials, or technology, without specified arrangements or safeguards? Has it detonated a nuclear device after August 3, 1977 although not a "nuclear-weapon State" under the nonproliferation treaty?* — 17. No.

18. FAA Sec. 901. Has the country denied its citizens the right or opportunity to emigrate? — 18. No.

B. FUNDING CRITERIA FOR COUNTRY

1. Development Assistance Country Criteria — **Not Applicable**

a. FAA Sec. 102(c), (d). Have criteria been established, and taken into account, to assess commitment and progress of country in effectively involving the poor in development, on such indexes as: (1) small-farm labor intensive agriculture, (2) reduced infant mortality, (3) population growth, (4) equality of income distribution, and (5) unemployment.

b. <u>FAA Sec. 104(d)(1)</u>. *If appropriate, is this development (including Sahel) activity designed to build motivation for smaller families in programs such as education in and out of school, nutrition, disease control, maternal and child health services, agricultural production, rural development, and assistance to urban poor?*

c. <u>FAA Sec. 201(b)(5), (7) & (8); Sec. 208; 211(a)(4), (7)</u>. Describe extent to which country is:

(1) Making appropriate efforts to increase food production and improve means for food storage and distribution.

(2) Creating a favorable climate for foreign and domestic private enterprise and investment.

(3) Increasing the public's role in the developmental process.

(4) (a) Allocating available budgetary resources to development.

(b) Diverting such resources for unnecessary military expenditure and intervention in affairs of other free and independent nations.

(5) Making economic, social, and political reforms such as tax collection improvements and changes in land tenure arrangements, and making progress toward respect for the rule of law, freedom of expression and of the press, and recognizing the importance of individual freedom, initiative, and private enterprise.

(6) Otherwise responding to the vital economic, political, and social concerns of its people, and demonstrating a clear determination to take effective self-help measures.

d. <u>FAA Sec. 201(b), 211(a)</u>. Is the country among the 20 countries in which development assistance loans may be made in this fiscal year, or among the 40 in which development assistance grants (other than for self-help projects) may be made?

e. <u>FAA Sec. 115</u>. Will country be furnished, in same fiscal year, either security supporting assistance, or Middle East peace funds? If so, *has Congress specifically authorized such use of funds, or* is assistance for population programs, humanitarian aid through international organizations, or regional programs?

2. <u>Security Supporting Assistance Country Criteria</u>

a. <u>FAA Sec. 502B</u>. Has the country engaged in a consistent pattern of gross violations of internationally recognized human rights? Is program in accordance with policy of this Section?

2.a. No. The program is in accordance with the policy of this Section.

b. <u>FAA Sec. 531</u>. Is the Assistance to be furnished to a friendly country, organization, or body eligible to receive assistance?

b. Turkey is a friendly country.

c. <u>FAA Sec. 533(c)(2)</u>. *Will assistance under the Southern African Special Requirements fund be provided to Mozambique, Angola, Tanzania, or Zambia? If so, has President determined (and reported to the Congress) that such assistance will further U.S. foreign policy interests?*

c. Not applicable.

d. <u>FAA Sec. 609</u>. If commodities are to be granted so that sale proceeds will accrue to the recipient country, have Special Account (counterpart) arrangements been made?

d. Not applicable.

e. <u>App. Sec. 113</u>. *Will security assistance be provided for the purpose of aiding directly the efforts of the government of such country to repress the legitimate rights of the population of such country contrary to the Universal Declaration of Human Rights?*

e. No.

f. <u>FAA Sec. 620B</u>. *Will security supporting assistance be furnished to Argentina after September 30, 1978?*

f. No.

ANNEX B

A.I.D. Loan No. 277-K-104

TURKEY: BALANCE OF PAYMENTS LOAN

AGREEMENT, dated the ________ day of ______________, 1978 between the Government of Turkey ("Borrower") and the United States of America, acting through the Agency for International Development ("A.I.D.").

WHEREAS, the Government of Turkey is presently experiencing serious economic problems;

WHEREAS, the Government of Turkey has taken a series of measures to overcome these problems and has entered into a stabilization program in conjunction with a Standby Agreement with the International Monetary Fund; and

WHEREAS, the Government of the United States, acting through the Agency for International Development, is desirous of supporting the Government of Turkey's efforts to stabilize its economy;

NOW, THEREFORE, the parties hereto agree as follows:

ARTICLE I

The Loan

A.I.D., pursuant to the Foreign Assistance Act of 1961, as amended, agrees to lend to the Borrower under the terms of this Agreement not to exceed Fifty Million United States Dollars ($50,000,000) for balance of payments financing to support and promote the financial stability and economic recovery of the Borrower. The aggregate amount of disbursements under the loan is referred to as "Principal".

ARTICLE II

Loan Terms

SECTION 2.1. Interest. The Borrower will pay to A.I.D. interest which will accrue at the rate of _____ percent (%) per annum following the date of disbursement of the Loan on the outstanding balance of principal and on any due and unpaid interest. Interest on the outstanding balance will accrue from the date of disbursement (as defined in Section 4.2) and will be payable semi-annually. The first payment of interest will be payable no later than six (6) months after disbursement of the Loan, on a date to be specified by A.I.D.

SECTION 2.2. Repayment. The Borrower will repay to A.I.D. the Principal within ten (10) years from the date of disbursement of the Loan in fifteen (15) approximately equal semiannual installments of Principal and interest. The first installment of Principal will be payable two and one-half ($2\frac{1}{2}$) years after the date on which the first interest payment is due in accordance with Section 2.1. A.I.D. will provide the Borrower with an amortization schedule in accordance with this Section after disbursement of the Loan.

SECTION 2.3. Application, Currency, and Place of Payment. All payments of interest and Principal hereunder will be made in U.S. Dollars and will be applied first to the payment of interest due and then to the repayment of Principal. Except as A.I.D. may otherwise specify in writing, payments will be made to the Controller, Office of Financial Management, Agency for International Development, Washington, D. C. 20523, U.S.A., and will be deemed made when received by the Office of Financial Management.

SECTION 2.4. Prepayment. Upon payment of all interest due, the Borrower may prepay, without penalty, all or any part of the Principal. Unless A.I.D. otherwise agrees in writing, any such prepayment will be applied to the installments of Principal in the inverse order of their maturity.

SECTION 2.5. Termination on Full Payment. Upon payment in full of the Principal and any accrued interest, this Agreement and all obligations of the Borrower and A.I.D. under it will cease.

ARTICLE III

Conditions Precedent to Disbursement

SECTION 3.1. Disbursement. Prior to disbursement under the Loan, the Borrower will, except as the Parties may otherwise agree in writing, furnish to A.I.D. in form and substance satisfactory to A.I.D.:

(a) an opinion of counsel acceptable to A.I.D. that this Agreement has been duly authorized, or ratified by, and executed on behalf of, the Borrower, and that it constitutes a valid legally binding obligation of the Borrower in accordance with all of its terms;

(b) a statement of the name of the person holding or acting in the office of the Borrower specified in Section 6.2.

SECTION 3.2. Notification. When A.I.D. has determined that the conditions precedent specified in Section 3.1 have been met, it will promptly notify the Borrower.

SECTION 3.3. Terminal Date for Conditions Precedent. If all the conditions specified in Section 3.1 have not been met within ninety (90) days from the date of this Agreement, or such later date as A.I.D. may agree in writing, A.I.D., at its option, may terminate this Agreement by written notice to Borrower.

ARTICLE IV

Disbursements

SECTION 4.1. Deposit of Disbursements. After satisfaction of conditions precedent, A.I.D. will deposit the proceeds of the Loan in a bank in the United States designated in writing by the Borrower.

SECTION 4.2. Date of Disbursement. Disbursement by A.I.D. will be deemed to occur on the date A.I.D. makes disbursement to the Bank to be named in Section 4.1.

SECTION 4.3. Terminal Date for Requesting Disbursement. Except as A.I.D. may otherwise agree in writing, the terminal date for requesting disbursement of the loan proceeds shall be six months from the date of this Agreement.

ARTICLE V

Use of Funds

SECTION 5.1. The Borrower agrees that the proceeds of the loan will be used for balance of payments financing and will not be used for financing military requirements of any kind, including the procurement of commodities or services for military purposes.

ARTICLE VI

Miscellaneous

SECTION 6.1. Communications. The Borrower undertakes to provide to A.I.D. such information relating to the economic and financial situations and related problems of the Borrower as may be necessary. Any notice, request, document or other communication submitted by either Party to the other under this Agreement will be in writing or by telegram or cable, and will be deemed duly given or sent when delivered to such party at the following address:

To the Borrower:

Ministry of Finance
Government of Turkey
Ankara, Turkey

To A.I.D.:

U.S. Ambassador
American Embassy
Ankara, Turkey

All such communications will be in English, unless the Parties otherwise agree in writing. Other addresses may be substituted for the above upon the giving of notice. The Borrower, in addition, will provide the U.S. Embassy in Ankara with a copy of each communication sent to A.I.D.

SECTION 6.2. Representatives. For all purposes relevant to this Agreement, the Borrower will be represented by the individual holding or acting in the office of Minister of Finance and A.I.D. will be represented by the U.S. Ambassador, each of whom, by written notice may designate additional representatives. The names of the representatives of the Borrower, with specimen signatures, will be provided to A.I.D., which may accept as duly authorized any instrument signed by such representatives in implementation of this Agreement, until receipt of written notice of revocation of their authority.

IN WITNESS WHEREOF, the Borrower and the United States of America, each acting through its duly authorized representative, have caused this Agreement to be signed in their names and delivered as of the day and year first above written.

GOVERNMENT OF TURKEY

By: ________________________

Title: ______________________

UNITED STATES OF AMERICA

By: ________________________

Title: ______________________