Implementation of Section 620(s) of the Foreign Assistance Act of 1961, as amended.

A Report to Congress for 1989/1990

The U.S. Agency for International Development

Washington, D.C. 20523

AGENCY FOR INTERNATIONAL DEVELOPMENT

320 TWENTY FIRST STREET, N.W.
WASHINGTON, D.C. 20523

March 1, 1991

The Administrator

The Honorable Thomas S. Foley
Speaker of the House of Representatives
Washington, D.C. 20515

Dear Mr. Speaker:

In accordance with Section 620(s) of the Foreign Assistance Act of 1961, as amended, I am pleased to transmit for the President the annual report for 1989/90 on the implementation of this provision.

Fifteen countries are cited in the report as appearing to have exceeded a comparative norm for military expenditures as compared to other countries regionally and worldwide. However, after examining these countries within their political, economic and security perspectives, no country is determined to be ruled out for assistance as a result of Section 620(s) considerations.

Sincerely,

Ronald W. Roskens

Enclosure: a/s

PHONE: (202) 647-9620 FAX: (202) 647-1770

AGENCY FOR INTERNATIONAL DEVELOPMENT

320 TWENTY FIRST STREET, N.W.
WASHINGTON, D.C. 20523

March 1, 1991

The Administrator

The Honorable Claiborne Pell
Chairman
Committee on Foreign Relations
United States Senate
Washington, D.C. 20510

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March 1, 1991

The Administrator

The Honorable Jesse A. Helms
Committee on Foreign Relations
United States Senate
Washington, D.C. 20510

Dear Senator Helms:

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Extract of FAA Legislation, Section 620(s)

Section 620(s) of the Foreign Assistance Act of 1961, as amended, states that:

(1) In order to restrain arms races and proliferation of sophisticated weapons, and to ensure that resources intended for economic development are not diverted to military purposes, the President shall take into account before furnishing development loans, Alliance loans or supporting assistance (economic support funds) to any country under this Act, and before making sales under the Agricultural Trade Development and Assistance Act of 1954, as amended:

> (A) the percentage of the recipient or purchasing country's budget which is devoted to military purposes; and
>
> (B) the degree to which the recipient or purchasing country is using its foreign exchange or other resources to acquire military equipment.

(2) The President shall report annually to the Speaker of the House of Representatives and the Committee on Foreign Relations of the Senate his actions in carrying out this provision.

Preface

Section 620(s) of the Foreign Assistance Act (FAA) of 1961, as amended, requires the President to report annually to the Speaker of the House of Representatives and the Senate Foreign Relations Committee on his actions in carrying out this requirement. The President's authority to administer this provision has been delegated through the Secretary of State and the Director of the International Development Cooperation Agency to the Administrator of the Agency for International Development (A.I.D.). The Administrator coordinates his report with other interested executive agencies which participate in the annual analyses of the nature of military expenditures by countries receiving assistance under the economic aid programs described herein.

In implementing Section 620(s), the executive agencies involved, including the A.I.D., the Departments of State and Defense, and the Arms Control and Disarmament Agency, examine the pattern of defense expenditures and military imports for each aid recipient country. To provide cross-country comparability, defense expenditures are expressed as a percentage of gross national product (GNP) and of central government expenditures, and military import figures are expressed as a percentage of total imports. These three measures and their rankings are shown in the regional and worldwide tables included in this report. Statistical data used in the report are from 1987, the most recent year for which the most complete statistics were available for preparing the 1989/90 report.

Because of statistical deficiencies and the difficulty of making comparisons among disparate country methods of accounting, budget systems, and definitions of defense costs, the statistical analysis is used primarily to establish a checklist for Section 620(s) reporting purposes.

The report for 1989/90 cites the following fifteen countries which appeared to have exceeded the norm for military expenditures, as compared to other countries regionally and worldwide. Political, economic and security considerations were taken into account in this analysis. Based on this review, it was concluded that considerations under Section 620(s) do not rule out assistance for these cited countries.

620(s) Countries

Countries annotated below with an asterisk were not included in last year's report.

Africa	Asia, the Near East and Europe	Latin America
Burundi	*Cyprus	Peru
*The Gambia	Egypt	
Mozambique	India	
*Tanzania	Israel	
	Jordan	
	Morocco	
	Oman	
	Pakistan	
	*Poland	
	Republic of Yemen	

COUNTRY SUMMARIES

Section 620(s) of the Foreign Assistance Act
of 1961, as Amended

Africa

Burundi

Since 1987, Burundi has been governed by the military regime of Major Pierre Buyoya. The Buyoya regime has adopted a policy of national reconciliation to address ethnic violence in that country between the minority Tutsis, who have traditionally exercised sovereignty over the majority Hutus. Following the last major ethnic incident in August 1988, the Buyoya government appointed an ethnically balanced cabinet and a Commission for National Unity to help resolve Burundi's ethnic problems. Prospects for a new constitution and economic and political reform in Burundi are forthcoming. On the military side, increased military expenditures since 1986 are attributed to efforts to defuse the 1988 ethnic violence and to help repatriate refugees.

The Gambia

The Gambia has a pluralistic democratic government and a commendable human rights record. Under President Jawara, The Gambia has implemented a model economic reform program which is fully supportive of the development objectives of the United States and other international donors. In 1989 the Senegambia Confederation, a mutual defense pact between Senegal and The Gambia, was dissolved. The Gambia's increased military expenditures are attributable to the development of The Gambian National Army during the Confederation period and the need to sustain its military during the period leading up to dissolution of the Confederation. The Gambia is a new country listed in this year's report.

Mozambique

Mozambique continues to face a major insurgency from RENAMO (Mozambique National Resistance) guerrillas. The situation has been compounded by drought. High host country military expenditure has been described by the Chissano government as necessary to protect civilians, maintain national sovereignty and continue national development efforts. Economically, Mozambique achieved a 4 percent rate of growth in its gross domestic product (GDP) in 1989 and is dismantling its socialist state apparatus.

Tanzania

Tanzania is a new 620(s) country. President Ali Hassan Mwinyi continues to liberalize the country from socialist policies to market-based economic adjustment. Since the launching of Tanzania's economic reform program in 1986, the country's economy has begun to show signs of recovery. Tanzania is important to the stability of eastern and southern Africa. Moreover, it is a front line state and has helped the Mozambican government against the RENAMO insurgency. Tanzania's increased military expenditures are partially attributable to continuing military support to anti-apartheid groups.

Asia, the Near East and Europe

Cyprus — U.S. assistance to Cyprus demonstrates concern for the people of Cyprus, and symbolizes active U.S. promotion of a durable settlement through aid for bicommunal activities. There is no indication that economic or social development in the Republic of Cyprus is being constrained by defense spending. Cyprus does not receive any military assistance from the United States, which explains the high military expenditure ratio in that country.

Egypt — Egypt's strategic location and its willingness to assume the role of a stabilizing force in the region place a relatively heavy defense burden upon it. As we have seen with the current Gulf crisis, Egypt's ability to respond effectively to outside force is a necessary condition for security in that region. Even with substantial U.S. aid, Egypt's efforts to modernize its armed forces place a heavy financial burden on its government.

India — India is a country faced with serious security concerns and plays a key role in maintaining regional peace and stability. Its long coastline requires investment in a sizable navy to patrol its borders. India's large military expenditures are also attributed to its desire to increase self-reliance in arms production and maintain peace in light of its hostile neighbors. India, however, is the world's largest democracy and a leader in the Non-Aligned Movement.

Israel — U.S. commitment to Israel's security and well-being has been a cornerstone of our Middle East policy since the creation of the State of Israel in 1948. Israel's high level of defense expenditures reflect its continuing concern over the potential threat posed by its neighbors, particularly Syria. Moreover, the Intifada uprising in the West Bank and Gaza has caused some increase in Israeli defense expenditures. Economically, Israel is now implementing a second phase of its structural adjustment program in order to improve the country's international competitiveness and long-term growth prospects.

Jordan — Jordan is situated on major air and land routes to the Persian Gulf oil-producing countries. Jordan also shares the longest border of any state with Israel; it continues to ensure tranquility along the border. Jordan must maintain sufficient defensive strength to deter threats by those opposing its moderate policies. Jordan is now facing a serious economic crisis as a result of the Gulf crisis.

Morocco — Morocco's military expenditures are attributable to its expenses incurred in the Saharan war and the country's need for military modernization. Also, new policies aimed at structural economic reform have curtailed other government expenditures, with the result that military expenses accounted for a rising share of budget resources.

Oman — Oman's strategic location on the Strait of Hormuz and its willingness to cooperate in regional security affairs makes it crucial to U.S. interests in the Gulf. Continuing tensions in the Persian Gulf and on Oman's border with Yemen highlight the need to strengthen Oman's defense capabilities.

Pakistan — In 1989, Pakistan was our key partner in South Asia. Pakistan's security environment improved with the end of the Iran-Iraq war, the withdrawal of Soviet troops from Afghanistan, and the continuing dialogue between the Indian and Pakistani governments. This improved environment and the deterioration of Pakistan's balance of payments encouraged the Bhutto government to review its defense budget.

Poland — Dramatic reforms in Poland reflect a process of political and economic democratization with profound international political implications. The statistical data for military expenditures reflect Poland's past obligations under the Warsaw Pact. Poland's strategic location as a buffer between the Soviet Union and Western Europe and its inclusion in the Soviet bloc have dictated heavy contributions by Poland to regional defense expenditures, including costs for supporting Soviet troops stationed in Poland. It is expected that under the new political arrangements in Eastern Europe, these levels will decrease.

Republic of Yemen

In the past year, the Yemen Arab Republic and Marxist People's Democratic Republic of Yemen (PDRY) succeeded in uniting. The newly constituted Republic of Yemen occupies a strategic position at the mouth of the Red Sea, and has long and unresolved borders with Saudi Arabia and traditionally tense relations with Oman. Historically a fairly stable, economically progressive country, North Yemen had contributed to regional stability. United Yemen is one of the poorest Arab countries and the most populous on the Arabian Peninsula. Deteriorating relations with Saudi Arabia because of Gulf crisis policy differences have led to a cut off of Saudi aid, the departure of 750,000 Yemenis from Saudi Arabia, and a serious economic crisis. Given the short-term crisis and prospects for longer-term disruptions in the region, Yemen could play a pivotal political and military role in the region.

Latin America and the Caribbean

Peru — Peru recently held fair and free presidential and legislative elections, but the stability of Peru is threatened by a violent insurgency, narcotics production and trafficking, and severe economic conditions. The continued support of the Peruvian armed forces is essential to protect the democratic process in Peru and to counter narcotics.

COUNTRY NARRATIVES

Section 620(s) of the Foreign Assistance Act
of 1961, as Amended

AFRICA

Burundi

Burundi is a small country (27,900 square kms.) with a population of about 5 million and a per capita income of $240. The country is landlocked and densely populated, (the second highest population density in Africa) with scarce natural resources other than its relatively fertile agricultural land. The society is primarily rural, with only 5 percent of the population living in urban centers. Agriculture (commercialized and subsistence) accounts for approximately 50 percent of GDP and provides employment and income for about 85 percent of the population. Coffee is the main export, generating four-fifths of total export earnings.

After a period of relatively good performance during the late 1970s, Burundi's economic and financial situation took a turn for the worse in the early 1980s, as a result of substantial deterioration of the terms of trade, expansionary fiscal and monetary policies, and adverse climatic conditions. Real GDP growth, which had averaged 5.1 percent per year during 1978-81, declined to less than one percent per year during 1982-84. In 1984, the external current account deficit reached a record high of 16 percent of GDP, and the overall fiscal deficit rose to 12 percent of GDP. Inflation ran at 14 percent a year, leading to a rapid appreciation of the Burundi franc. In response to these problems, the Government of Burundi, with the cooperation of the IMF and the World Bank, undertook an economic stabilization and structural reform program in 1986 that continues to be among the most effective in Sub-Saharan Africa.

For most of Burundi's recorded history, political power has been held by the minority Tutsi ethnic group which exercised its sovereignty over the majority Hutu group (85% of the population) through a feudal relationship. While Hutus have always enjoyed some possibilities for upward mobility, their socio-economic status has historically been inferior to the Tutsis. This situation was exacerbated by the colonial regime's policy of giving opportunities for higher education and civil service almost exclusively to Tutsis. Ethnic consciousness increased in the years before independence, particularly with the outbreak of the first tribal violence in Rwanda in 1959.

Hutu awareness of, and frustration with, discrimination was heightened by independence in 1962 which, unlike in Rwanda where the Hutu gained control of the government, provided them only expanded political power within the context of a Tutsi constitutional monarchy. The inability of the Hutus to wield real power despite a majority in the National Assembly caused their frustrations to erupt into violence in 1965. This uprising was met with bloody repression, inaugurating a pattern that has been repeated in 1969, 1972, and again in much modified form, in 1988.

Since the overthrow of the monarchy by the Tutsi-dominated army in 1966, successive military leaders have pledged themselves to ease ethnic tensions. However, it was not until September 1987, with the coming to power (by bloodless coup) of Major Pierre Buyoya, that the Government of Burundi made ethnic reconciliation its top priority. The eruption of ethnic violence in August 1988 served to accelerate the process of ethnic reconciliation as the Buyoya government moved rapidly to restore peace and to address long festering tribal differences. It appointed an ethnically balanced cabinet as well as a Commission for National Unity composed of Hutu and Tutsi leaders to study ways to resolve the ethnic problem. The Commission called for sweeping changes, including the reestablishment of democratic institutions, the elimination of discriminatory employment practices, educational reform, and the creation of a national body to oversee the operations of the security forces. The government is now implementing these recommendations and is awaiting the Commission's constitutional charter which will serve as the basis for a new constitution. The new constitution, along with current and anticipated economic and political reforms, is expected to improve significantly the Hutus' status in the economy and society and will, hopefully, return the government to civilian control.

Most of the increased military expenditures since 1986 were the result of the change in government that took place in 1987, which led to increased military salaries; extensive government efforts to defuse the ethnic violence that erupted in August 1988, and large scale government efforts, often utilizing military equipment and resources, to resettle repatriated refugees and to ensure that areas of potential ethnic tension remain calm. During 1989, drought-related food shortages and the continuing use of military resources and equipment to distribute emergency food contributed to existing military spending.

Conclusion: Considerations under Section 620(s) do not rule out assistance.

The Gambia

The Gambia is an English-speaking nation located on the Atlantic Coast of west Africa. With a total area of only 11,000 square kilometers and a population of approximately 800,000, The Gambia has one of the highest population densities in Africa. The country forms an enclave within Senegal extending 350 kilometers eastward along both sides of the Gambia River.

The country's geography is an accident of political history: control of the Gambia River, the most navigable waterway in West Africa, was retained by the British for strategic reasons, while surrounding territories were colonized by the French. As a consequence, The Gambia cuts across the settlements of about a dozen different tribes, most of which are present in Senegal.

With its history of free and fair elections and leadership in international human rights forums, The Gambia has demonstrated a commitment to multi-party democracy and the rule of law. As a trading nation, with a recently liberalized market economy, The Gambia provides an example of the potential for growth in Africa through economic reform.

The economy of The Gambia is predominantly agricultural with groundnut products accounting for 70 percent of the country's domestically produced exports. Production of subsistence crops --primarily millet sorghum, rice and maize--covers approximately 75 percent of national consumption requirements; commercial imports cover the remaining 25 percent.

The Gambia is heavily dependent on trade and has an active commercial sector. All fuel and capital goods, most manufactured items, and a significant amount of food must be imported. The country's coastal location and liberal trade policy have enabled The Gambia to serve as a commercial entrepot for much of the region. Imported items are re-exported to Senegal, Mali, Guinea-Bissau, Mauritania, and other countries, and account for up to 75 percent of total exports. The Gambia's small size, dependence on commercial trade, and heavy reliance upon a single domestically produced export crop render the economy highly vulnerable to external factors, particularly volatile terms of trade, regional trade relationships, and shortfalls in rainfed agricultural production.

Between 1985 and 1990 The Gambia successfully implemented one of the most comprehensive structural adjustment programs in sub-saharan Africa. Under the program, price distortions and structural imbalances in the economy were largely eliminated and notable macroeconomic improvements were realized. Despite successive years in which GDP growth has averaged between 4 and 5.5 percent, annual per capita income in 1990 is still only $225, and The Gambia remains among the world's poorest countries. Behind the macroeconomic achievements, people-level impacts of the stabilization program have been slow to materialize: illiteracy rates remain high; access to adequate health care and housing is limited; basic food security is precarious; most roads are unpaved; supply of water and electricity is at best irregular; and, the economy has been unable to generate sufficient employment opportunities to meet demand. At the present rate of growth, doubling of per capita income to $450 per year would not be accomplished until the year 2024.

In 1981, after a coup attempt by leftist elements in the country was quelled by Senegalese troops invited in by the government, The Gambia entered into a mutual defense pact with Senegal for military assistance. The two countries signed a series of protocols establishing the Senegambia Confederation which committed these two nations to expanded mutual defense and national security arrangements, the establishment of joint foreign policy organizations, and the eventual integration of the two economies. During the confederation period, The Gambia pursued the development of The Gambian national army which included the 150-man contribution to a confederal battalion as stipulated in the Senegambian agreement. A Gambian gendarmerie (modeled after the Senegalese counterpart) was established under the Minister of Defense.

Other than the development of the security services, very little happened during the confederation. Meetings of cabinet officials from each nation took place to discuss problems of mutual interest. The confederation was eventually dissolved in 1989. Thus, most of the increased military expenditures in The Gambia can be attributed to the creation and dissolution of the confederation and the need for The Gambia to meet its military obligations under the Pact and later, unilaterally, to fully fund its own military and security forces. In the future, these military increases will probably remain moderate because of civil service personnel retrenchment and expenditure restrictions stipulated in IMF and World Bank structural adjustment agreements with the government.

<u>Conclusion</u>: Considerations under Section 620(s) do not rule out assistance.

Mozambique

Since 1980, the Government of Mozambique has faced a major armed uprising involving RENAMO (Mozambique National Resistance) guerrillas. The insurgency has severely damaged the nation's economic and social infrastructure, and the situation has been compounded by drought.

Primarily as a result of civil conflict, over two million Mozambicans have been internally dislocated from their homes and another million have fled to neighboring countries as refugees. Civilians are a primary RENAMO target, and tens of thousands of innocent citizens have died in the conflict. Altogether, close to 7.6 million persons out of a population of 15 million are affected by the emergency. A massive international relief effort has been mounted to feed those facing food shortages.

The nationwide insurgency has also led to the destruction of transportation networks, power distribution, and agricultural production. In this context, the relatively high military expenditures of Mozambique have been described by the government as necessary to protect civilians, maintain national sovereignty, and continue national development efforts.

To counter the active insurgency and restore stability, President Chissano has mounted a major effort to increase the nation's military capabilities. This effort involves reorganizing the military and securing additional military equipment to protect food convoys. At present, the Mozambican military cannot guarantee the safety of civilians in the countryside. Mozambique's neighbors and European allies have been increasing military aid to Mozambique, and at present Western advisors outnumber those of the Soviet bloc. At the same time, the government is attempting to secure a peaceful end to the conflict. President Chissano has initiated peace talks with RENAMO through Kenyan and Zimbabwean mediators. The government has made significant human rights progress over the past two years.

Despite the insurgency, Mozambique is making economic progress and achieved a 4.0 percent GDP growth rate last year. Through the Program for Economic Rehabilitation (PRE), the government decisively set about the task of dismantling the centralized economic apparatus of the socialist state. The PRE included several devaluations, wage and price increases, layoff of government workers, and investments in smaller private economic units. Mozambique has agreed with the IMF and the World Bank on a structural adjustment program and sold off many state farms and enterprises. Both the IMF and the World Bank are pleased with the seriousness of Mozambican economic reform efforts.

Because of Mozambique's key position in the region, the success of our efforts to promote peace and stability in southern Africa depends importantly on how we handle our relations with Mozambique and respond to its needs. The U.S. Government's policy of constructive relations with Mozambique and our bilateral humanitarian and development assistance have bolstered a conscious decision by the Government of Mozambique to have peaceful accommodation with its neighbors, move toward genuine non-alignment on international issues, and pursue difficult internal reforms. By encouraging these steps through our diplomacy and economic assistance, we have advanced prospects for regional peace and stability. At the same time, we have used our influence to promote political reforms in Mozambique. In July 1989, the ruling FRELEMO party officially abandoned Marxism as the guiding national philosophy. On January 9, 1990, Mozambique unveiled a new constitution which provides for direct elections of the president and national assembly and for greater guarantees of individual rights. This new constitution was ratified by Parliament in November 1990 and is now in effect. On January 24, 1990, President Bush signed a Presidential Determination to remove Mozambique from the list of Marxist-Leninist countries prohibited from receiving EXIM Bank loans and guarantees.

Additional assistance to Mozambique is consistent with our broader objective of promoting economic progress in the region. Mozambique has been a key supporter of U.S. efforts to promote regional peace and stability and has embarked on diplomatic initiatives to expand ties with South Africa. This moderating role among the Front Line States establishes a useful model of regional cooperation.

U.S. military assistance to Mozambique is prohibited by law. The U.S. assistance program in Mozambique in FY 1989 consisted of $55.7 million in humanitarian and food relief, $34.5 million for a regional rail project, and $18.9 million in development assistance, keyed to the private sector. Our efforts are designed to improve private agricultural production and implement economic reforms.

Conclusion: Considerations under Section 620(s) do not rule out assistance.

Tanzania

Tanzania is adopting a less ideological, more pragmatic stance among the Front Line States, which is contributing to stability in eastern and southern Africa. The willingness of the Government of Tanzania to continue to reorient the economy from socialist policies to more market-oriented principles is a another positive factor for U.S. interests in the region.

The government's emphasis on equity over efficiency enabled Tanzania to realize significant gains in basic education and health in the 1970s and early 1980s. However, two decades of excessive government controls and intervention by inefficient parastatals resulted in the decline and subsequent stagnation of the Tanzanian economy. The country's infrastructure is seriously eroded, and the overall standard of living has yet to recover from its fall in the late 1970s.

In 1986, with support of the IMF and the World Bank, the Government of Tanzania launched an economic reform program. As part of that program, the government eliminated controls on food crop marketing, thus allowing the private sector to purchase crops. As a result of economic policy changes, the economy began to show signs of recovery: export earnings were up 11 percent in 1988/89, and GDP growth of over 4 percent in 1987 and 1988 constituted the first increases in per capita income this decade.

The U.S. is a relatively minor donor in Tanzania, contributing less than one percent of official development assistance in 1987. At present, the main thrust of U.S. assistance to Tanzania is to support development efforts in transport and population, two critical sectors to Tanzania's economic growth and social well-being. Improvements in transportation services for domestic and neighboring country exporters will facilitate access of producers to inputs and markets, thus supporting economic activity and growth. The U.S. aid program in Tanzania also supports a family planning program to help reduce the country's 3.3 percent population growth rate that threatens to erase the hard-won gains of the past three years. The United States is also supporting modest activities in wildlife conservation, AIDS education and control, and human resource development.

Tanzania presently enjoys peaceful relations with her neighbors but must maintain vigilance on the southern border because of the war in Mozambique. As a Front Line State, Tanzania sent 112,000 troops to Mozambique to help in the war against RENAMO. While the troops were withdrawn in 1988, it is likely that that expedition, as well as continuing military support to anti-apartheid groups such as the African National Congress and Pan African Congress, are responsible for the increased volume of military imports. In 1988, for the first time, the United States began a modest military training program with Tanzania.

Conclusion: Considerations under Section 620(s) do not rule out assistance.

ASIA, NEAR EAST AND EUROPE

Cyprus

Cyprus has a long history of good economic performance characterized by relatively high growth, low unemployment, price stability, and external balance. This good performance was severely disrupted by the hostilities of 1974, but thereafter rapid economic growth was resumed and full unemployment was again achieved by the end of 1978. Today, per capita income for the 550,000 persons in the southern part of the country is estimated to be about $8,000. In the north, living standards of the population of 150,000 persons are below those of the south, and per capita income is approximately $2,000.

Growth of gross domestic product (GDP) during 1974-1984 averaged over 6.0 percent per annum but slowed to 3.2 percent during 1985-1986. This slowdown was due partly to supply constraints in certain sectors and to the economic recession in the Middle East oil-exporting countries, which adversely affected Cyprus' major exports, namely clothing, leather goods, and cement. Reflecting declining inflation in Cyprus' main trading partners and lower domestic wage demand, inflation as measured by the consumer price index declined from 11 percent in 1981 to about 3 percent in 1987.

The statistical data for 1987 indicate that Cyprus spent 2.9 percent of its central government budget on defense--equivalent to 0.9 percent of the country's gross national product (GNP). Approximately 17.5 percent of the country's imports were military. While the Republic ranks fourth in military imports as a percentage of total imports, it ranks 55 and 53, respectively, in defense expenditures as a percent of GNP and of central government expenditures. There is no indication that economic or social development in the Republic of Cyprus is being constrained by defense spending.

U.S. economic assistance to Cyprus consists entirely of economic assistance to promote cooperation between Greek and Turkish-Cypriot communities and to encourage and support bicommunal confidence-building projects. These objectives are consistent with Section 620C of the Foreign Assistance Act of 1961, as amended, and do not raise any arms control concerns.

Conclusion: Considerations under Section 620(s) do not rule out assistance.

Egypt

The statistical data for 1987 show that Egypt spent 22.3 percent of its central government expenditures on defense. This was equivalent to 9.2 percent of GNP. By comparison, in 1986 defense-related expenditures as a percent of central government expenditures (28.1 percent) and of GNP (14.2 percent) were higher than in 1987. As a percent of total imports, however, Egypt's military imports in 1987 (13 percent) were higher than they were in 1986 (9.2 percent).

Egypt's strategic location and its willingness to assume the role of a stabilizing force in the region places a heavy defense burden upon it. As we have seen with the current Gulf crisis, Egypt's ability to respond effectively to outside force is deemed necessary for the security of the region. Iraqi military might and the invasion of Kuwait pose an immediate threat to Egypt which has long worked to promote moderation and mutual security amongst regional states. A possible threat exists from a hostile Libyan Government on its western border, although efforts have recently been made to stabilize political relations. A potential threat also exists from Iran due to Egypt's support of more moderate regimes in the Persian Gulf area. To assure its own defense and meet its responsibilities as a stable force in the region, Egypt has embarked on a program to replace outmoded Soviet defense equipment with modern Western weapons. This accounts for the relatively high proportion of imports of military materials, largely from the United States. Even with substantial assistance from the United States, this revamping and upgrading of defense capability continues to place an extremely heavy financial responsibility on the Government of Egypt.

Over the past five years, Egyptian economic growth has slowed, due largely to inefficient use of its considerable economic resources and a decline in the growth of external resources. Rigidities in the prices of food and other commodities and extensive government controls over production activities have caused major imbalances in the structure of the economy, as investors and decision markers reacted to improper signals. Until the mid-1980's, the counter-productive and costly effects of these policies were largely masked by strong increases in the inflows of external resources. During the last five years, however, stagnant or declining levels of external inflows, coupled with rising debt service obligations and an inadequate economic policy framework, are placing great pressure on Egypt's budget, balance of payments, and economic growth prospects.

Egypt's debt servicing burden was temporarily alleviated over the 1987-88 period through a multilateral Paris Club rescheduling exercise facilitated by an IMF stand-by arrangement. As part of the IMF stand-by arrangement, Egypt began a phased program to merge the multiple exchange rates and implemented a significant increase in energy prices. Reforms in energy, food and agriculture pricing, and liberalization of controls in agriculture have continued, but the overall pace of other reforms has slowed. As a result, balance of payments and budgetary disequilibria have worsened. With a new IMF agreement under negotiation, Egypt is again facing the original payment schedules on nearly $50 billion in external debt.

Recent U.S. military debt forgiveness, totalling nearly $8 billion, has proved beneficial to Egypt's economic situation. A more rapid pace of economic reform is needed, however, to restore equilibrium and economic growth. To the extent that economic adjustments succeed in stimulating the economy, present levels of defense spending need not interfere with economic development objectives. However, if needed policy reforms are not implemented more rapidly, the Egyptian government's widening deficits will become untenable in the short-to medium-term. Budget austerity in all fields remains a part of the IMF recommended strategy for the Egyptian economic reform program, and the A.I.D. program has been encouraging and supporting policy improvements. Egypt has been forced to keep all new defense purchases made with hard currency or foreign loans to an absolute minimum, relying predominantly on grants of U.S. Foreign Military Sales equipment.

Conclusion: Considerations under Section 620(s) do not rule out assistance.

India

India is a country faced with serious security concerns. Its long coast line alone requires investment in a sizable navy to patrol its borders. Since independence, when the country was partitioned, India has been involved in three wars with Pakistan, and tension between the two states has been an endemic condition. Each country is pursuing a nuclear program which increases the suspicions of the other. India also has stationed troops on its northern border with China. This presence is strong, and tension along this border remains a political issue.

Despite a lack of political consensus on many national issues, the Indian political elites are united in the belief that India must be a regional military power and are willing to pay the costs of developing that power. The consensus among its policy-makers, that India must be militarily strong and able to defend itself, fuels the fear internally that it may have to rely on other countries for its military equipment. Having experienced an arms embargo during one of its wars with Pakistan, India now has a declared policy to become militarily self-sufficient.

In the mid-1980's, India weathered one of its worst droughts, an event which just 20 years ago would have spelled economic and human disaster on a massive scale. India's resilience in the face of the drought is the best recent evidence we have of the remarkable development progress it has made since its independence. This includes virtual self-sufficiency in food grain production and the improvement of socio-economic conditions--with life expectancy increasing by 33 percent, literacy by nearly 90 percent, and infant mortality declining from 146 per thousand live births to 90 per thousand. Macroeconomic performance improved to 4.9 percent GDP growth per year in the 1980's--particularly unfavorable years for LDC growth globally. The deepening of its institutional and human resource base and the increasing sophistication of India's response to many of its most pressing development problems are critical factors underlying these achievements. As a sign of its commitment to the country's development, India budgeted $273 billion in its current 5-year plan. India will cover 90 percent of these development costs from internal resources.

Notwithstanding these achievements, India remains one of the world's poorest countries, with 40 percent of its people below the poverty line, a stubbornly persistent population growth rate above 2.0 percent, and an increasing strain on its natural resources.

Conclusion: Considerations under Section 620(s) do not rule out assistance.

Israel

Israel's economy grew rapidly until the early 1970's. Through high levels of investment and with a highly skilled labor force, Israel has developed a modern industrial state whose citizens enjoy a standard of living comparable to that of southern Europe. Israel's boom ended in the mid-1970's in the face of higher oil prices and in the wake of the 1973 war when a major share of the country's resources were diverted to defense.

While the Egypt-Israeli peace treaty brought peace between these two countries, Israel's high level of defense expenditures reflect its continuing concern over the potential threat posed by its neighbors, particularly Syria and Iraq. The Intifada (uprising in the West Bank and Gaza) has caused some increase in Israeli defense expenditures along with some slowdown in growth.

From early in the 1980's, high levels of defense spending, coupled with high levels of private consumption led to increased demand for goods and services. Since domestic production could not simultaneously satisfy all of the demand for these services, the unsatisfied demand led to fiscal deficits, increased imports, and deficits in the external goods and services accounts. Financing the fiscal deficit led to triple-digit inflation in the early 1980's. Balance of payments deficits have been financed by massive U.S. assistance, private transfers, concessional lending, and foreign commercial borrowing.

Faced with a crisis that threatened to wipe out its foreign exchange reserves, the Government of Israel launched an Economic Stabilization Program (ESP) in 1985. The ESP was a watershed in recent Israeli economic history. Key elements of that program include reduction in price controls and some subsidies, wage restraint, reduction or limitations in other government expenditure, devaluation, and tight monetary policy. The ESP resulted in the reversal of the balance of payments current account, from a $1.5 billion deficit in 1984 to a $1.5 billion surplus in 1986. However, by 1987, the current account was again in deficit by over $900 million, due in part to a reduction in unilateral transfers, but mainly to a doubling of military imports. The current account deficit narrowed to $675 million in 1988 as the pressure of military purchases subsided.

Having achieved a degree of economic stability, the Government of Israel now faces other key decisions. The long-term health of the Israeli economy will depend upon success in continuing implementation of a second phase of structural adjustment aimed at improving the country's international competitiveness and long-term growth prospects. Targets include a shift in emphasis from short-term stabilization to a long-term growth strategy; further progress in controlling inflation; maintaining a realistic exchange rate; continued progress in cost reduction through increased labor productivity and by taking advantage of recently moderating wage demands; steady improvements in the private investment and savings climate which would include lower real interest rates; reduced regulatory impediments to private investment, and continued rapid progress in the privatization of public enterprise.

Israel faces an enormous economic challenge, absorbing a projected one million Soviet immigrants over the next several years. The Israeli economy is struggling to provide housing and jobs. The GOI estimates that absorbing these immigrants will require 600,000 new jobs, 250,000 additional housing units, and added infrastructure investment of $10 billion over the next five years. To finance the absorption, the Government of Israel projects GDP must grow at 8.35% versus the current rate of 3%, exports must more than double, and billions of dollars in investment capital must be found over normal requirements and receipts.

The United States maintains close security ties with Israel, and the U.S. assistance program is designed to help Israel deal with both its economic and military problems. Since FY 1986 the amounts of Foreign Financing credit and economic assistance have been maintained at $3 billion annually. Beginning in FY 1985, all such assistance has been provided as grants. In 1988 the Israeli Government converted $4.75 billion of its debt to the U.S. Government by selling bonds in the U.S. capital market and, as a result of this refinancing, it is estimated that the Government of Israel is able to save more than $100 million in annual interest payments. U.S. economic assistance, however, cannot substitute for the continuation and strengthening of the stabilization program which Israel initiated in 1985, and for policies and programs designed to establish conditions conducive to self-sustaining growth.

<u>Conclusion</u>: Considerations under Section 620(s) do not rule out assistance.

JORDAN

The Government of Jordan continues to provide assurances that it is actively seeking to enforce sanctions against Iraq in the Gulf crisis. It continues as a force for moderation and stability in the Middle East. Jordan serves as a key player in the search for progress towards resolution of the Arab-Israeli conflict, despite its withdrawal from most administrative ties with the West Bank in July 1988. Price riots in April 1989 prompted Jordan to hold its first parliamentary elections in 22 years. The elections were free and open. In 1989, the government took several steps toward further political liberalization, such as freeing up the press and the release of some political detainees. In 1990 more pluralistic reforms were made involving the completion of the national charter (which may pave the way for legitimation of political parties) and the partial lifting of martial law. Jordan has entered the front ranks of countries in the Arab world moving toward a more democratic, representative government.

Jordan has prevented attacks against Israel from its border, the longest of any of Israel's Arab neighbors. Jordan's own security situation continues to be precarious because of the uncertainties occasioned by Iraq's aggression in the Gulf. Jordan's defensive capability relative to Syria has declined dramatically during the last decade. While progress on the initial construction of the Unity Dam indicates some improvement in bilateral relations, press reports indicate that Syria has allowed an increasing number of infiltrations through Jordan directed against Israel over the past year.

Jordan's military resources have been stretched in an attempt to keep the Jordanian-Israeli border quiet and protected from such incursions. Jordan must maintain sufficient defensive strength to deter threats by those opposing its moderate policies. Jordan's military must also be prepared to cope with civil disturbances which could be a long-or short-term result of the Gulf crisis.

Jordan's economy suffered severely in recent years, and future prospects for growth are bleak given the current situation in the Gulf. Its principal sources of foreign exchange have declined: Gulf-based workers' remittances, Arab and other donor aid flows, and phosphate export earnings. Moreover, the Gulf crisis has imposed unexpected hardship on Jordan's economy due to the impact of half a million refugees flowing though the country and more than 100,000 staying in Jordan. Unemployment now ranges to 30 percent, and the labor force is expanding at 4-5 percent a year. GNP growth turned negative in 1987 and

1988, implying a steady loss in real per capita income as population grew at 3.6 percent a year. In 1988 and 1989 the government was in serious budgetary deficit; foreign exchange reserves were at their lowest levels in Jordan's history; and, Jordan's debt service was at its highest ever. (1990 and 1991 will be even worse.)

As recently as 1989 Jordan demonstrated its resolve to adjust to these economic troubles by liberalizing the economy; stimulating foreign investment and export; discouraging luxury imports; allowing more flexible interest rate policies; allowing the Jordanian Dinar to float (and thereby to depreciate by 50 percent); and advancing a market-oriented strategy which promotes private enterprise as the engine for growth and employment. The Gulf crisis has caused the economy to spiral downwards, however, and the government is currently out of compliance with its stand-by arrangement with the IMF. Although Jordan has started receiving some emergency assistance, the situation in the region is grave and remains unstable.

Conclusion: Considerations under Section 620(s) do not rule out assistance.

MOROCCO

The latest available statistics (1987) indicate that Morocco spent 20 percent of its government budget on defense, or 7.1 percent of Gross National Product. Military imports were 3.1 percent of total imports. These figures are not inordinately large in view of the expenses of the Saharan war and the need for military modernization, but they do require an explanation pursuant to the requirement of Section 620(s) of the Foreign Assistance Act.

Military expenditures increased by less than 3 percent in 1987. However, new policies aimed at structural economic reform curtailed other government expenditures, especially investment, with the result that military expenses accounted for a rising share of budget resources, giving the appearance of rising military expenses in real terms. Given Morocco's participation in the international coalition against Iraq, it is not likely that military expenditures will decline in Morocco.

The United States and Morocco have enjoyed many years of military and economic cooperation. Moreover, Morocco has made important facilities available to the United States and has participated in joint training exercises. The United States has long assisted in upgrading Morocco's defense infrastructure. There are plans to continue that military assistance.

The Government of Morocco has made a strong commitment to economic reform and growth, and the positive results of the new economic regime are being felt. Helped by substantial exchange rate depreciation and other structural adjustment policies, the external current account deficit was reduced from 12 percent of GDP in 1982 to a surplus of 2.1 percent in 1988. A major feature of this progress was a rapid expansion in manufacturing exports. Inflation has been brought down from 10 percent to 2 percent during the same period and the fiscal deficit from 12 percent of GDP to 4-5 percent. Yet, real economic growth has only been moderately satisfactory at about 4 percent annually. U.S. assistance has contributed to Moroccan economic growth, both in real terms and in technical assistance, which has prepared the policy framework for large-scale infusion of IBRD financing.

Conclusion: Considerations under Section 620(s) do not rule out assistance.

OMAN

The economy of Oman is closely linked to the petroleum industry, and oil has contributed well over 90 percent of GDP in recent years. Continued soft prices for oil through 1989 have precipitated a marked decline in government revenues with the budget shifting from a substantial surplus to deficit spending since 1983. The projected deficit for the 1989 budget is over $1 billion, despite efforts to trim recurrent spending. Sectors of the economy, closely linked to government spending, have experienced a sharp downturn. For example, the contribution of the construction industry to GDP fell 38 percent in 1987. The manufacturing and fishing sectors have shown improvement, partly a result of the high priority placed on diversification to reduce economic dependence on oil.

Regional and national security concerns have been the driving force behind Oman's security expenditures in the past. The current instability in the Persian Gulf does not offer the rationale to change Oman's existing defense expenditure patterns. The Iran-Iraq conflict posed direct risk to Oman, given the proximity to Iran and the vulnerability of crucial oil infrastructure and shipping.

The United States has had a closer military relationship with Oman since the implementation of the Access Agreement in 1980. Although there has been no military assistance under FMS since 1986 and International Military Education and Training (IMET) has been maintained at a minimal level, Oman continues to benefit from increased security derived from the U.S. military presence.

The Government of Oman has demonstrated a strong commitment to the economic development and modernization of the country and has invested oil revenues heavily in a broad range of domestic programs, including efforts to diversify the economy and reduce petroleum dependence. A.I.D. programs are managed through the Omani-American Joint Commission and support high-priority activities in water resources, fisheries, and educational development. National economic development is clearly the top priority of the Omani Government. Security expenditures rose in response to overt external threats and instability in the region. Given the continuing insecurity in the region, military expenditures are not expected to lessen in the short-term.

Conclusion: Considerations under 620(s) do not rule out assistance.

PAKISTAN

Pakistan sustained solid growth through 1989 despite military expenditures, a continued global economic slowdown, and the enormous burden imposed by the Afghan refugees. Pakistan's real growth averaged nearly 7 percent from 1983 to 1986, but fell to 5.7 percent in 1986-87, 5.8 percent in 1987-88, and 5.1 percent in 1988-89.

Pakistan's balance of payments position deteriorated significantly in Pakistani fiscal year 1989, primarily due to an adverse shift in the terms of trade. The overall trade deficit increased 2 percent to $2.6 billion. More positively, foreign exchange remittances from Pakistani workers abroad and from international and bilateral donors, which had decreased at a fairly steady annual rate of 12 percent in recent years, declined only 6 percent in that country's FY 1988-89 from Pakistani workers in the Gulf. This favorable trend in remittances ceased abruptly in Pakistan in FY 1990, as Pakistani workers flocked home following Iraq's invasion of Kuwait. At the end of the fiscal year, Pakistan's foreign exchange reserves were $452 million, roughly 3.3 weeks of imports.

The deterioration in Pakistan's export position was primarily due to lower production and export of rice and in the unit value of raw cotton and cotton yarn. The relatively smaller increase in the import bill was due primarily to lower than expected imports of fertilizer and petroleum, and to relatively stable international oil prices. The Bhutto government projected some improvement in the balance of payments position during Pakistan's FY 1990, due to expectations for improved export growth, and a decline in imports. (However, in Pakistani FY 1990, the balance of payments situation unraveled primarily due to the crisis in the Gulf.)

Federal budget deficits were a source of continued concern because large public borrowing had fueled inflation. The budgets presented by the Bhutto Government in June 1989 and June 1990 contained a number of measures--including an expanded sales tax and improved tax administration procedures intended to increase revenues.

In 1989, Pakistani authorities were concerned that the country's defense capability had not grown as fast as the offensive capabilities of neighboring India, Iran and Afghanistan. Throughout 1989 the Soviets continued to supply the Kabul regime with large quantities of modern weapons, including combat aircraft and ballistic missiles, a number of which have affected Pakistani territory. India continued to expand and modernize its armed forces and now has one of the largest military establishments in the world. Iran used its petroleum earnings for massive arms purchases during its war with Iraq and continues aggressively to export its radical ideology.

As of 1989, Pakistan's security environment had improved with the end of the Iran-Iraq war, the withdrawal of Soviet troops from Afghanistan, and the continuing dialogue between the Indian and Pakistani governments (which deteriorated again in 1990 as regional tensions increased over Kashmir). This improved environment and the deterioration of Pakistan's balance of payments encouraged the Pakistani Government to reevaluate its defense budget. Several expensive, high-tech systems were dropped from the GOP's list of possible defense acquisitions under discussion with the United States. In 1989, the Bhutto government made a strong public commitment to devoting more of the available public resources to increasing the education and welfare of the average citizen. At the same time, however, pressure from the military and a strong conservative political opposition kept the pressure on the Bhutto government to not reduce defense spending.

The development of Pakistan's nuclear capability continues to be of concern to the United States. Certification was made in 1989. Since October 1, 1990, the USG has been unable to certify, under the Pressler Amendment, that Pakistan does not possess a nuclear device.

Conclusion: Considerations under Section 620(s) do not rule out assistance.

POLAND

The statistical data for 1988 show that Poland spent 31.7 percent of its central government budget for defense. This was equivalent to 6.9 percent of GNP. Approximately 12 percent of the country's imports were for military expenditures, primarily from the Soviet Union.

These data reflect Poland's obligations under the Warsaw Pact. Poland's strategic location, as a buffer between the Soviet Union and Western Europe and its inclusion in the Soviet bloc, has dictated participation in regional defense organizations. Under the Warsaw Pact, Poland has been obligated to contribute heavily to regional defense expenditures, including costs for supporting Soviet troops stationed in Poland.

Poland's economic problems have worsened considerably over the past years, in part owing to high central government outlays including defense expenditures. Beginning in August, with the advent of a Solidarity-led government in Poland, the government has become committed to a comprehensive program of economic and political reforms. The Polish Government entered into an agreement with the IMF in December 1989 which resulted in various stabilization measures. A decrease in military expenditure is now part of the Polish Government's commitment to reduce the budget deficit. For 1989/90, only 3.6 percent of GNP was anticipated to be spent on defense.

U.S. assistance to Poland was initially supported through the Support for East European Democracy (SEED) Act of 1989. The SEED Act supports substantive steps toward institutionalizing political democracy and economic pluralism in Eastern Europe. In view of strategic U.S. considerations, the movement toward democracy and free market economic policies in Poland is of significance to the political stability of Europe, the end of the Cold War and ultimately to world peace.

U.S. assistance to Poland is not only earmarked for specific objectives, but is also facilitated with "notwithstanding" provisions to enable A.I.D. to implement the program more effectively.

Conclusion: Considerations under Section 620(s) do not rule out assistance.

REPUBLIC OF YEMEN

Yemen occupies a strategic position on the entrance to the Red Sea and shares borders with Saudi Arabia and Oman. The Yemen Arab Republic and the People's Democratic Republic of Yemen unified on May 22, 1990. Security concerns in Yemen are derived in part from historical internal friction--since the overthrow of the theocratic regime of the Imamate in 1962, two of Yemen's five presidents have been overthrown and two were assassinated. The Yemeni Government does not have total authority over fiercely independent tribal factions. In the past, the unstable relationship with the Marxist regime in PDRY resulted in a number of armed clashes. Maintenance of a strong defensive capability is likely to remain a high priority in Yemen over the near term because of a significant deterioration in relations with Saudi Arabia since the onset of the Gulf crisis.

The Republic of Yemen is faced with formidable economic problems which have recently reached near crisis proportions in terms of foreign exchange reserves and the ability to make debt payments. Yemen's difficulties are exacerbated by unification and the return of 750,000 Yemenis from Saudi Arabia, with a concomitant severe loss of worker remittances. Though the Yemen Arab Republic began exporting oil at the end of 1987, oil income has been modest and has not come close to offsetting declines in other sources of foreign exchange. The result has been a severe shortage of foreign exchange, growing current account deficits and increased inflationary pressure. Yemen's halting movement toward an outwardly oriented economic development process has left the country with a substantial deficit of modern economic and social infrastructure and the economic problems mentioned above, which coupled with a high population growth rate, have slowed the modernization of the country.

Despite the problems mentioned above, Yemen has made substantial progress in addressing social and physical infrastructure requirements. Yemen's national planners have demonstrated an increasingly sophisticated appreciation of the priorities for economic development and of the role of the private sector as the primary engine for stimulating growth. The expanded role of elected representatives to parliament following elections in mid-1988 is expected to provide an additional forum for discussion of national development priorities. Multi-party parliamentary elections are scheduled for 1992.

Security concerns will likely result in continued emphasis on national defense, although defense expenditures are not expected to rise as a percent of overall expenditures in the future. The military is currently trying to merge the defense forces of the former North and South Yemens. Despite the relatively high level of military expenditures, Yemen has tried to minimize the budgetary impact by negotiating to extend or forgive military assistance loans. Future fiscal austerity measures will have an impact on both defense and economic development budgets, but it is clear that Yemen is placing a high priority on devoting budgetary resources, especially scarce foreign exchange, to development efforts.

Conclusion: Considerations under Section 620(s) do not rule out assistance.

LATIN AMERICA AND CARIBBEAN

PERU

Peru is currently at a critical juncture in its economic, political, and social history. Peruvian democratic stability is threatened by economic depression, a violent insurgency and narcotics trafficking.

Politically inexperienced Alberto Fujimori, a first generation Japanese and virtually unknown until mid-March 1990, defeated internationally known novelist Mario Vargas Llosa and was inaugurated president of Peru on July 28, 1990. Fujimori's election represented the Peruvian people's rejection of the European elite who dominated Peruvian political and economic life as well as the economic "shock" program of his opponent, Mario Vargas Llosa. Fujimori and his government are anxious to improve relations with the United States.

Although he achieved an overwhelming majority of the popular vote, Fujimori's ability to govern is constrained first, by the inexperience of his government and second, by his party's lack of a majority in Congress (only 25 percent). Fujimori has, however, launched several bold campaigns (from family planning to penal reform) against powerful interests while maintaining public support.

Peru's economy is in shambles following years of financial mismanagement. Peru has been a pariah in international financial lending circles since 1987 following former President Garcia's decision to cease debt servicing. The Fujimori government entered office facing the unenviable task of stabilizing a depressed, hyperinflationary economy; introducing painful structural reforms; and reestablishing constructive relations with the international financial community. Within days after his inauguration, Fujimori announced the first stage of his economic program. The stabilization measures, far more drastic than expected, focused on short-term fiscal policies and have successfully reduced inflation. Peru is currently discussing a medium-term growth program with the IMF and IBRD but significant problems remain, not the least the question of Peru's sizeable arrearages.

In this context, the Peruvian armed forces is providing a strong supportive role in sustaining democracy by attempting to contain the spread of subversion while performing its traditional peacetime function of protecting the integrity of Peru's borders. These efforts are being carried out in the context of a deteriorated economic situation that has severely curtailed the availability of adequate budgetary resources.

Long oriented toward external threats, the Peruvian military is ill-equipped to meet the challenges posed by subversive movements, and expenditures are indeed real. The country is in fact facing the classic guns versus butter dilemma. U.S. interests and objectives in Peru are at stake in the resolution of this dilemma. First is the preservation of democracy. Meeting this objective requires that the military be provided with adequate levels of resources to field an army that can meet the challenges posed by subversion. Yet, achieving this objective also requires that the populace be provided with sustained and adequate levels of income through the allocation of scarce resources to economic activities.

The dilemma is also extended to another fundamental objective: the suppression of narcotrafficking. While currently concentrating its scarce resources on the insurgency, the new government and its military are showing increased interest in pursuing anti-narcotics activities. Effective interdiction requires the allocation of increased resources to the military. However, the economic effects on the populace of reduced income resulting from the suppression of narcotics also cannot be ignored.

The U.S. approach to this dilemma is to encourage the Peruvian authorities to strike a judicious balance in their allocation of resources to defense and economic activities. In this context, we have emphasized the need to have a stable economy that could serve as a solid base upon which efforts to meet security and welfare needs can be built. Focused emphasis in either security or welfare will not be conducive to the preservation of democracy in Peru.

In this context, the suspension of U.S. economic assistance on the basis of past levels of defense expenditures would be counter-productive. It would signal a withdrawal of U.S. support to a sieged democracy, and would seriously set back U.S. efforts to suppress narcotrafficking.

Conclusion: Considerations under Section 620(s) do not rule out assistance.

APPENDIX

METHODOLOGY FOR PREPARATION OF SECTION 620(s)

In implementing Section 620(s), the executive agencies involved examine the pattern of defense expenditures and military imports for each aid recipient country. To provide cross country comparability, defense expenditures are expressed as a percentage of gross national product and of central government expenditures. Similarly, military import figures are expressed as a percentage of total imports.

The three resulting measures and their rank are presented in worldwide and regional tables. All figures in this report refer to 1986 or 1987, the latest years for which the most complete statistics were available for preparing the 1988-89 report.

SOURCE

The source of data used throughout this report is the U.S. Arms Control and Disarmament Agency (ACDA), as reported in its publication, World Military Expenditures and Arms Transfer, 1988.

DEFINITION OF DATA ELEMENTS

Defense Expenditures	Data on NATO country military expenditures (defense expenditures) are based on NATO definitions. In summary, civilian-type expenditures of each NATO defense ministry are excluded and military-type expenditures of other ministries are included; grant military assistance is included in the expenditures of the donor country; and purchases for credit are included at the time the debt is incurred, not at the time of payment. For other non-communist countries, data are generally the expenditures of the ministry of defense. When these are known to include the costs of internal security, an attempt is made to remove these expenditures. It should be

recognized that the data are of uneven accuracy and completeness. There are indications that the military expenditures reported by some countries consist mainly or entirely of recurring or operating expenditures and omit all or most capital expenditures, including arms purchases. In the case of several countries -- Algeria, Cuba, Ecuador, Egypt, Honduras, Iraq, Iran, Libya, and Syria -- special note of this possibility is made in Table I of ACDA's 1988 World Military Expenditures Report (see Source).

Gross National Product Gross National Product (GNP) represents the total output of goods and services produced by residents of a country and valued at market prices.

Central Government Expenditures Central Government Expenditures (CGE) include current and capital (developmental) expenditures plus net lending to government enterprises, by central (or federal) governments. It should be noted that for the Soviet Union, China, Iran, Jordan, and possibly others, the ratio of military expenditures to central government expenditures may be overstated, inasmuch as the estimate for military expenditures is obtained at least in part independently of nominal budget or government expenditure data, and it is possible that all estimated military expenditures do not pass through the nominal central government budget.

Military Imports Arms transfers (military imports) represent the international transfer (under terms of grant, credit, barter or cash) of military equipment, usually referred to as "conventional," including weapons of war, parts thereof, ammunition, support equipment, and other commodities designed for military use. Excluded are foodstuffs, medical equipment, petroleum products, and other supplies. Military services such as construction, training, and technical support are included for countries other than the United States. The statistics are estimates of the value of goods actually delivered during the reference year, in contrast both to the value of programs, agreements, contracts, or orders which may result in future deliveries, and to payments made during the period. Because countries may not include their arms imports or exports in their trade statistics, "total" imports and exports may be understated; in this event, ratios such as (estimated) arms imports to "total" imports will be overstated and may even exceed 100 percent.

*All definitions are taken from the Statistical Notes of ACDA's World Military Expenditures and Arms Transfers, 1988.

COUNTRIES WITH THE HIGHEST RANKINGS ON MEASURES INCLUDED IN SECTION 620(s) OF THE FOREIGN ASSISTANCE ACT OF 1961, AS AMENDED

Burundi

* Cyprus

Egypt

* The Gambia

India

Israel

Jordan

Morocco

Mozambique

Oman

Pakistan

Peru

* Poland

* Tanzania

Yemen Arab Republic

* Not included in last year's report

Africa

	Defense Expenditures as a percent of				Military Imports as a percent of Total Imports	
	Gross National Product		Central Government Expenditures			
	Pct.	Rank	Pct.	Rank	Pct.	Rank
BOTSWANA	2.2	19	3.8	24	0.0	31
BURKINA FASO	3.1	22	17.6	5	7.4	8
BURUNDI	3.1	12	12.7	9	9.4	4
CAMEROON	1.9	22	8.4	13	0.6	20
CAR.	.	.	.	.	0.0	31
CHAD	3.5	7	40.1	1	.	.
CONGO	4.6	3	12.5	10	.	.
COTE DIVOIRE	1.9	22	4.9	22	0.0	31
EQ. GUINAE	.	.	.	.	.	.
GAMBIA, THE	.	.	.	.	10.1	3
GHANA	0.9	25	6.2	18	0.6	20
GUINEA	.	.	.	.	8.8	5
GUINEA-BISSAU	3.2	10	4.1	23	.	.
KENYA	2.4	17	8.0	14	0.6	20
LESOTHO	.	.	.	.	0.0	31
LIBERIA	3.8	6	14.2	7	3.2	14
MADAGASCAR	2.4	17	7.2	15	6.0	10
MALAWI	1.4	23	5.1	21	0.0	31
MALI	2.5	15	.	.	8.1	7
MAURITANIA	4.2	5	.	.	0.0	31
MAURITIUS	0.2	29	0.8	26	0.0	31
MOZAMBIQUE	8.4	1	34.6	2	35.4	1
NIGER	0.7	27	5.7	19	.	.
NIGERIA	0.8	26	2.7	25	0.8	16
RWANDA	2.0	20	12.0	11	0.0	31
SENEGAL	2.2	19	6.7	17	0.6	20
SIERRA LEONE	0.5	28	.	.	0.0	31
SOMALIA	3.2	10	30.0	3	5.5	11
SOUTH AFRICA	4.4	4	14.7	6	0.0	31
SUDAN	2.7	14	7.0	16	5.2	12
SWAZILAND	1.3	24	5.1	21	0.0	31
TANZANIA	.	.	.	.	11.9	2
TOGO	3.3	8	13.3	8	.	.
UGANDA	.	.	.	.	8.4	6
ZAIRE	3.0	13	18.2	4	4.0	13
ZAMBIA	.	.	.	.	0.8	16
ZIMBABWE	5.0	2	11.6	12	6.6	9

ASIA

Europe and Near East

	Defense Expenditures as a percent of				Military Imports as a percent of Total Imports	
	Gross National Product		Central Government Expenditures			
	Pct.	Rank	Pct.	Rank	Pct.	Rank
BANGLADESH	1.8	17	26.4	3	0.4	18
CYPRUS	0.9	21	2.9	21	17.5	3
EGYPT	9.2	4	22.3	6	9.2	6
FIJI	1.2	20	4.1	20	0.0	22
HUNGARY	5.2	9	12.0	13	3.7	9
INDIA	3.9	11	16.9	12	19.1	2
INDONESIA	2.1	16	8.7	17	1.9	14
ISRAEL	16.6	2	24.7	5	11.1	5
JORDAN	13.9	3	22.0	7	11.8	4
LEBANON	.	.	.	.	0.3	19
MOROCCO	7.1	6	20.0	9	3.1	10
NEPAL	1.2	20	5.0	19	0.0	22
OMAN	23.3	1	43.4	1	1.6	16
PAKISTAN	6.5	8	25.4	4	2.6	12
PHILIPPINES	1.3	18	7.8	18	0.6	17
POLAND	6.9	7	31.7	2	6.5	8
PORTUGAL	3.2	13	9.7	14	0.1	20
SRI LANKA	3.1	15	9.4	15	1.9	14
THAILAND	3.7	12	18.3	11	2.7	11
TUNISIA	3.1	15	9.0	16	1.6	16
TURKEY	4.4	10	19.4	10	7.0	7
YEMEN ARAB REP	7.2	5	21.5	8	30.0	1

Latin America and Caribbean

	Defense Expenditures as a percent of Gross National Product		Defense Expenditures as a percent of Central Government Expenditures		Military Imports as a percent of Total Imports	
	Pct.	Rank	Pct.	Rank	Pct.	Rank
BARBADOS	0.6	11	1.8	10	3.9	4
BELIZE	•	•	•	•	•	•
BOLIVIA	3.0	4	16.6	3	0.0	10
COSTA RICA	0.6	11	2.2	9	0.0	10
DOMINICAN REP.	1.4	8	10.9	7	0.3	8
ECUADOR	2.6	5	15.3	4	3.4	5
EL SALVADOR	3.9	2	30.3	1	8.9	2
GRENADA	•	•	•	•	•	•
GUATEMALA	1.5	7	13.1	6	0.3	8
HAITI	1.8	6	9.6	8	•	•
HONDURAS	3.7	3	13.3	5	6.9	3
JAMAICA	1.1	9	•	•	0.4	6
PERU	4.9	1	24.8	2	12.5	1

World Rankings

	Defense Expenditures as a percent of				Military Imports as a percent of Total Imports	
	Gross National Product		Central Government Expenditures			
	Pct.	Rank	Pct.	Rank	Pct.	Rank
ALGERIA	3.0	50	8.3	57	5.9	34
ANGOLA	.	.	.	.	92.9	3
ARGENTINA	1.4	73	12.0	44	0.5	68
BAHRAIN	4.1	29	13.9	33	10.7	20
BANGLADESH	1.8	67	26.4	11	0.4	69
BARBADOS	0.6	87	1.8	83	3.9	38
BELIZE	.	.	.	.	.	.
BENIN	2.1	61	15.5	28	.	.
BOLIVIA	3.0	50	16.6	27	0.0	98
BOTSWANA	2.2	59	3.8	77	0.0	98
BRAZIL	0.8	84	6.2	67	0.6	66
BURKINA FASO	3.1	46	17.6	25	7.4	28
BURMA	3.0	50	20.9	20	3.7	40
BURUNDI	3.1	46	12.7	39	9.4	22
COTE DIVOIRE	1.9	65	4.9	73	0.0	98
CAMBODIA	.	.	.	.	.	.
CAMEROON	1.9	65	8.4	56	0.6	66
CAPE VERDE	.	.	.	.	.	.
C.A.R.	.	.	.	.	0.0	98
CHAD	3.5	37	40.1	3	.	.
CHILE	4.0	30	12.7	39	0.8	59
COLOMBIA	1.1	79	7.4	61	0.2	75
COMOROS	.	.	.	.	.	.
CONGO	4.6	25	12.5	40	.	.
COSTA RICA	0.6	87	2.2	82	0.0	98
CUBA	.	.	.	.	24.9	10
CYPRUS	0.9	82	2.9	79	17.5	12
DJIBOUTI	.	.	.	.	.	.
DOMINICAN REP.	1.4	73	10.9	47	0.3	74
ECUADOR	2.6	53	15.3	29	3.4	42
EGYPT	9.2	9	22.3	17	9.2	23
EL SALVADOR	3.9	32	30.3	8	8.9	24
EQ. GUINEA	.	.	.	.	.	.
ETHIOPIA	8.5	10	24.0	16	111.1	2
FIJI	1.2	77	4.1	76	0.0	98
GABON	4.8	24	7.6	60	0.0	98
GAMBIA, THE	.	.	.	.	10.1	21
GHANA	0.9	82	6.2	67	0.6	66
GREECE	6.2	17	12.0	44	1.1	55
GRENADA	.	.	.	.	.	.
GUINEA	.	.	.	.	8.8	25
GUINEA-BISSAU	3.2	42	4.1	76	.	.
GUYANA	.	.	.	.	.	.
HAITI	1.8	67	9.6	52	.	.
HONDURAS	3.7	35	13.3	36	6.9	30
HUNGARY	5.2	20	12.0	44	3.7	40
INDIA	3.9	32	16.9	26	19.1	11
INDONESIA	2.1	61	8.7	55	1.9	51
IRAN	.	.	.	.	15.7	13
IRAQ	.	.	.	.	75.5	4

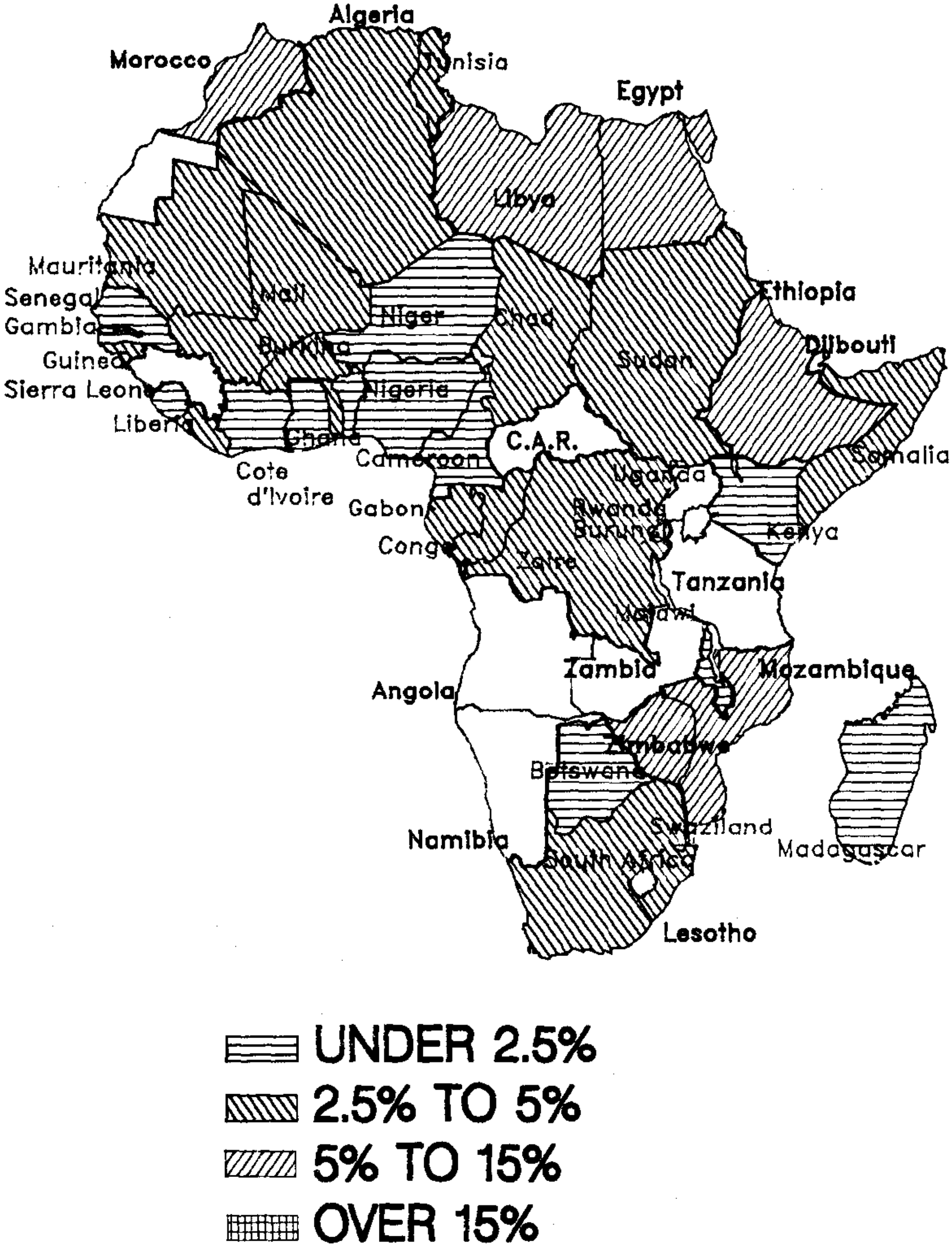
World Rankings

	Defense Expenditures as a percent of				Military Imports as a percent of Total Imports	
	Gross National Product		Central Government Expenditures			
	Pct.	Rank	Pct.	Rank	Pct.	Rank
ISRAEL	16.6	4	24.7	15	11.1	19
JAMAICA	1.1	79	.	.	0.4	71
JORDAN	13.9	5	22.0	18	11.8	18
KENYA	2.4	57	8.0	58	0.6	66
KOREA, REP. OF	4.8	24	25.5	12	1.3	54
KUWAIT	5.2	20	13.7	34	2.9	46
LAOS	.	.	.	.	39.0	6
LEBANON	.	.	.	.	0.3	74
LESOTHO	.	.	.	.	0.0	98
LIBERIA	3.8	33	14.2	32	3.2	44
LIBYA	11.1	8	.	.	12.8	15
MADAGASCAR	2.4	57	7.2	62	6.0	33
MALAWI	1.4	73	5.1	70	0.0	98
MALAYSIA	3.2	42	9.7	51	0.5	68
MALI	2.5	55	.	.	8.1	27
MALTA	1.5	70	3.7	78	0.0	98
MAURITANIA	4.2	28	.	.	0.0	98
MAURITIUS	0.2	90	0.8	84	0.0	98
MEXICO	0.5	89	2.3	81	1.9	51
MOROCCO	7.1	14	20.0	21	3.1	45
MOZAMBIQUE	8.4	11	34.6	5	35.4	7
NEPAL	1.2	77	5.0	71	0.0	98
NICARAGUA	.	.	.	.	54.2	5
NIGER	0.7	85	5.7	68	.	.
NIGERIA	0.8	83	2.7	80	0.8	59
OMAN	23.3	1	43.4	1	1.6	53
PAKISTAN	6.5	16	25.4	13	2.6	48
PANAMA	2.0	63	6.4	65	0.4	71
PAPUA NEW GUINEA	1.5	70	4.1	76	0.0	98
PARAGUAY	1.0	80	11.2	46	0.0	98
PERU	4.9	22	24.8	14	12.5	16
PHILIPPINES	1.3	75	7.8	59	0.6	66
POLAND	6.9	15	31.7	7	6.5	32
PORTUGAL	3.2	42	9.7	51	0.1	76
QATAR	.	.	.	.	0.0	98
RWANDA	2.0	63	12.0	44	0.0	98
SAUDI ARABIA	12.8	6	30.0	10	15.6	14
SENEGAL	2.2	59	6.7	64	0.6	66
SIERRA LEONE	0.5	89	.	.	0.0	98
SINGAPORE	5.5	18	15.1	30	0.6	66
SOUTH AFRICA	4.4	27	14.7	31	0.0	98
SRI LANKA	3.1	46	9.4	53	1.9	51
SUDAN	2.7	51	7.0	63	5.2	36
SURINAME	2.6	53	4.9	73	3.2	44
SWAZILAND	1.3	75	5.1	70	0.0	98
SYRIA	11.9	7	32.0	6	26.7	9
TANZANIA	.	.	.	.	11.9	17
THAILAND	3.7	35	18.3	23	2.7	47
TOGO	3.3	38	13.3	36	.	.

World Rankings

	Defense Expenditures as a percent of				Military Imports as a percent of Total Imports	
	Gross National Product		Central Government Expenditures			
	Pct.	Rank	Pct.	Rank	Pct.	Rank
TRINIDAD & TOBAGO	.	.	.	.	0.0	98
TUNISIA	3.1	46	9.0	54	1.6	53
TURKEY	4.4	27	19.4	22	7.0	29
U.A.E.	7.4	12	36.9	4	3.6	41
UGANDA	.	.	.	.	8.4	26
URUGUAY	2.5	55	10.1	49	0.0	98
VENEZUELA	3.6	36	10.7	48	1.0	56
VIETNAM	19.4	3	40.7	2	132.1	1
YEMEN AR REP(N)	7.2	13	21.5	19	30.0	8
YEMEN PDR (S)	22.0	2	.	.	.	.
ZAIRE	3.0	50	18.2	24	4.0	37
ZAMBIA	.	.	.	.	0.8	59
ZIMBABWE	5.0	21	11.6	45	6.6	31

DEFENSE EXPENDITURES AS A PERCENT OF GROSS NATIONAL PRODUCT



1987 DATA

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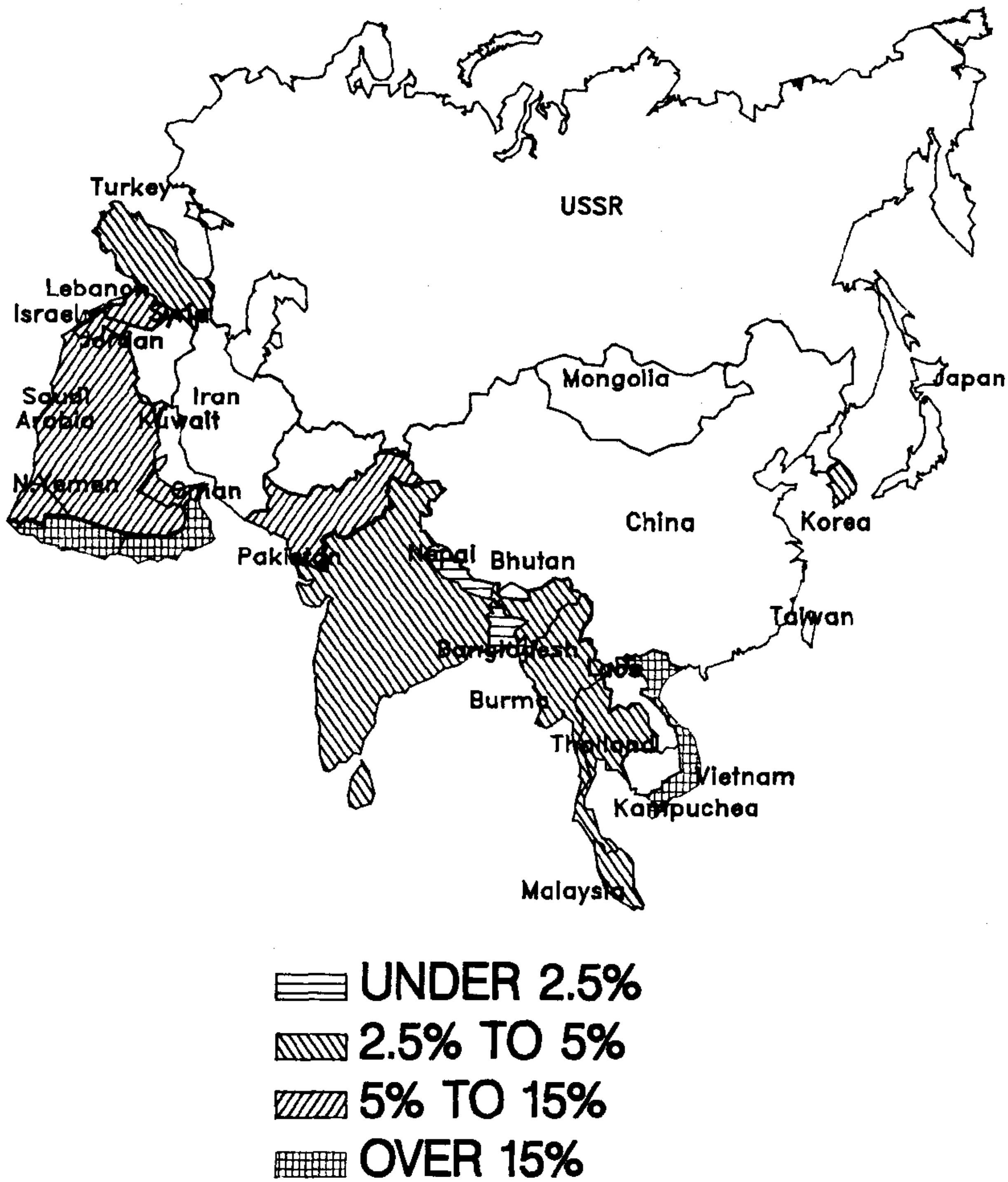
DEFENSE EXPENDITURES AS A PERCENT OF GROSS NATIONAL PRODUCT



1987 DATA

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DEFENSE EXPENDITURES AS A PERCENT OF GROSS NATIONAL PRODUCT

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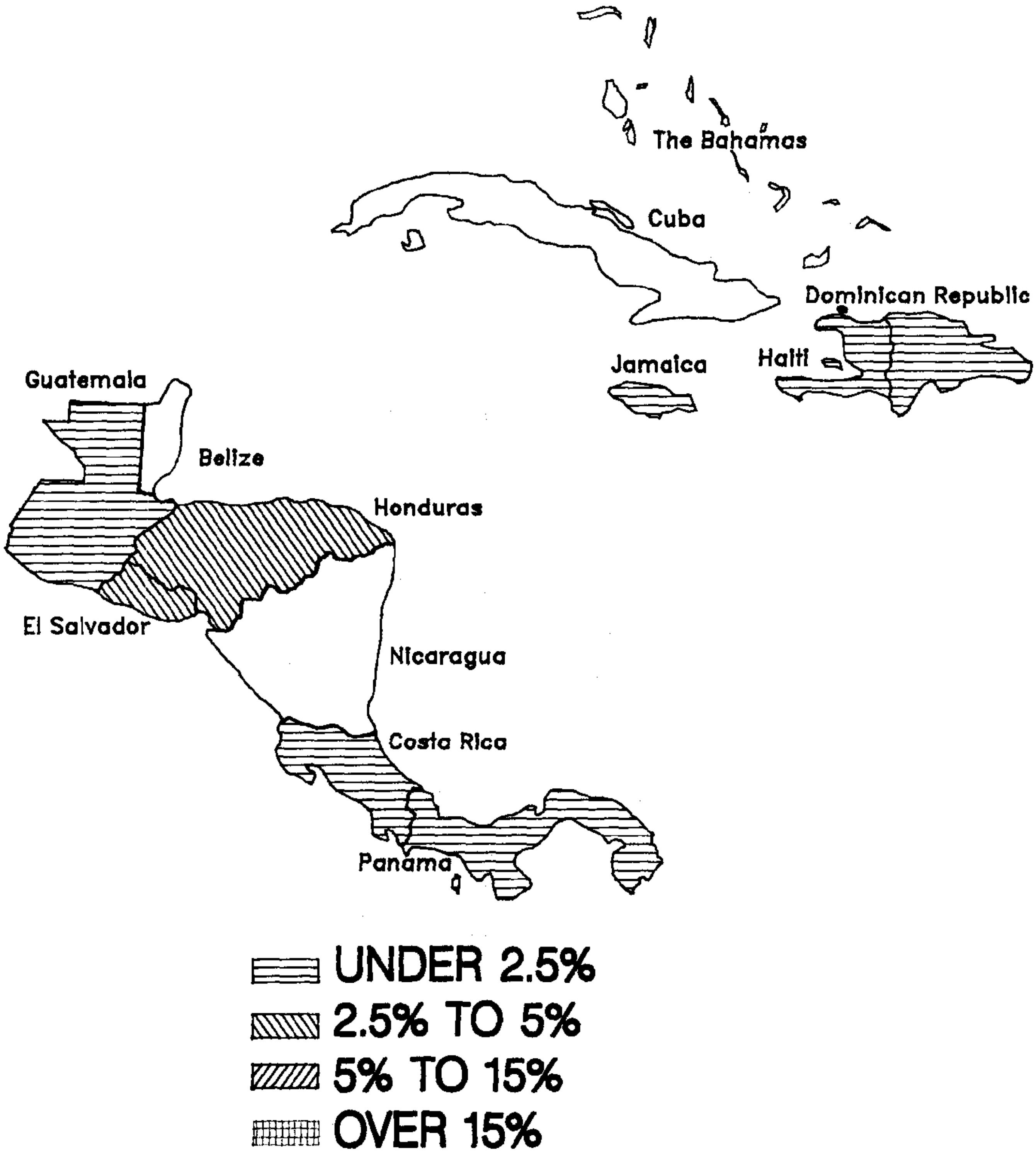
DEFENSE EXPENDITURES AS A PERCENT OF GROSS NATIONAL PRODUCT



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DEFENSE EXPENDITURES AS A PERCENT OF CENTRAL GOVERNMENT EXPENDITURES

UNDER 5% — 5% TO 10%

10% TO 20% — OVER 20%

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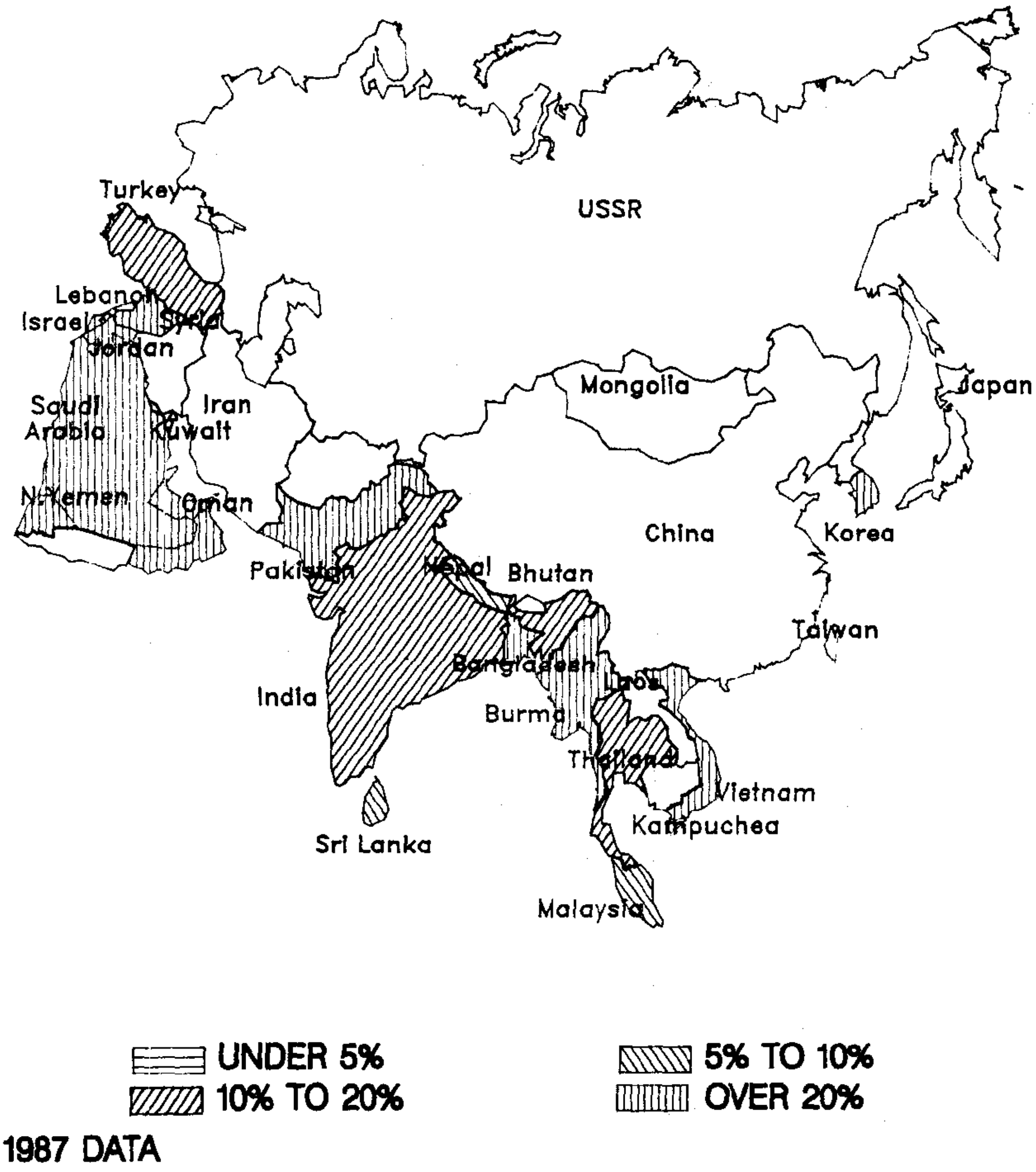
DEFENSE EXPENDITURES AS A PERCENT OF CENTRAL GOVERNMENT EXPENDITURES



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DEFENSE EXPENDITURES AS A PERCENT OF CENTRAL GOVERNMENT EXPENDITURES

UNDER 5% — 5% TO 10%
10% TO 20% — OVER 20%

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MILITARY IMPORTS AS PERCENT OF TOTAL IMPORTS

UNDER 2.5%
2.5% TO 5%
5% TO 15%
OVER 15%

1987 DATA
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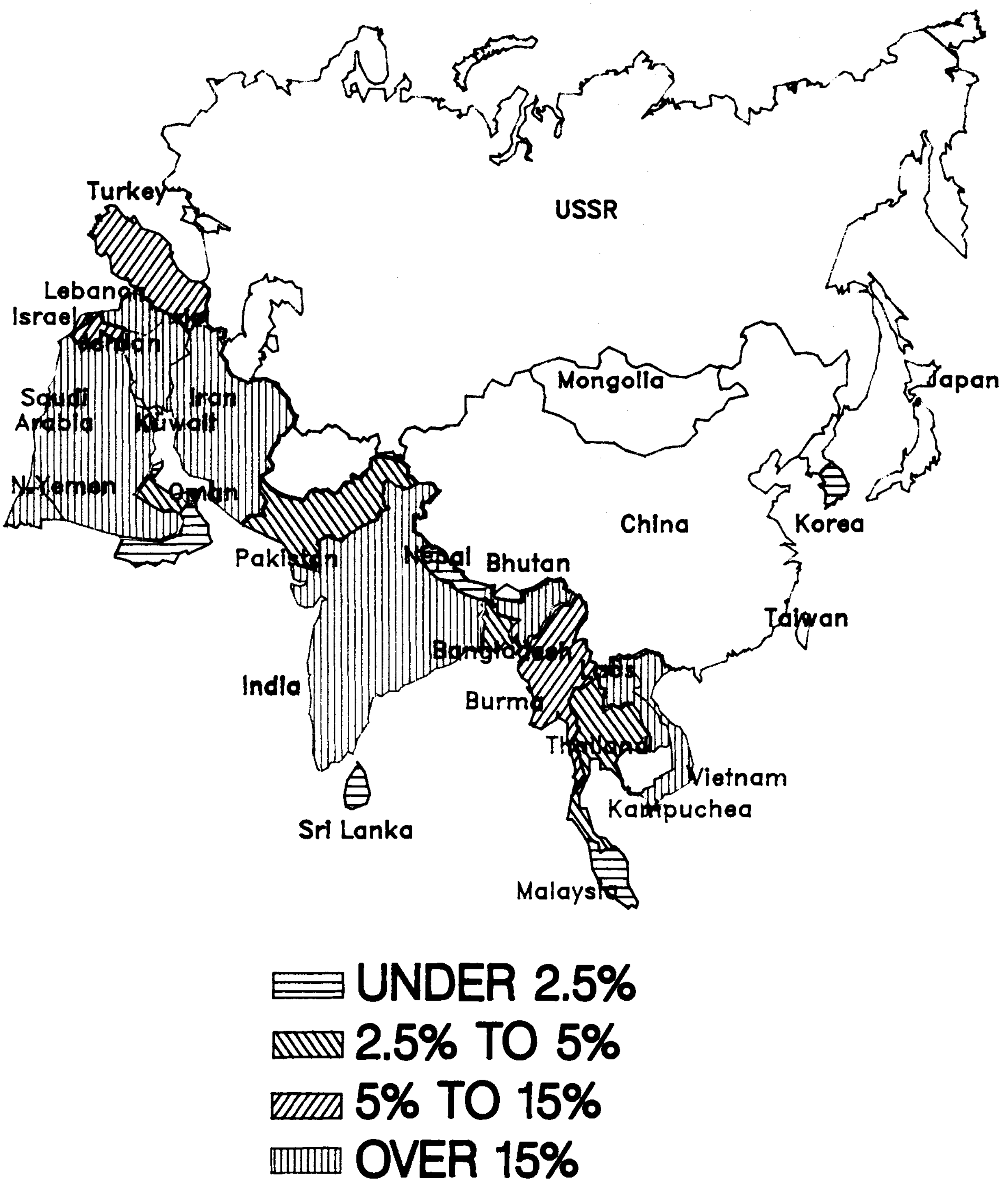
MILITARY IMPORTS AS PERCENT OF TOTAL IMPORTS



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MILITARY IMPORTS AS PERCENT OF TOTAL IMPORTS

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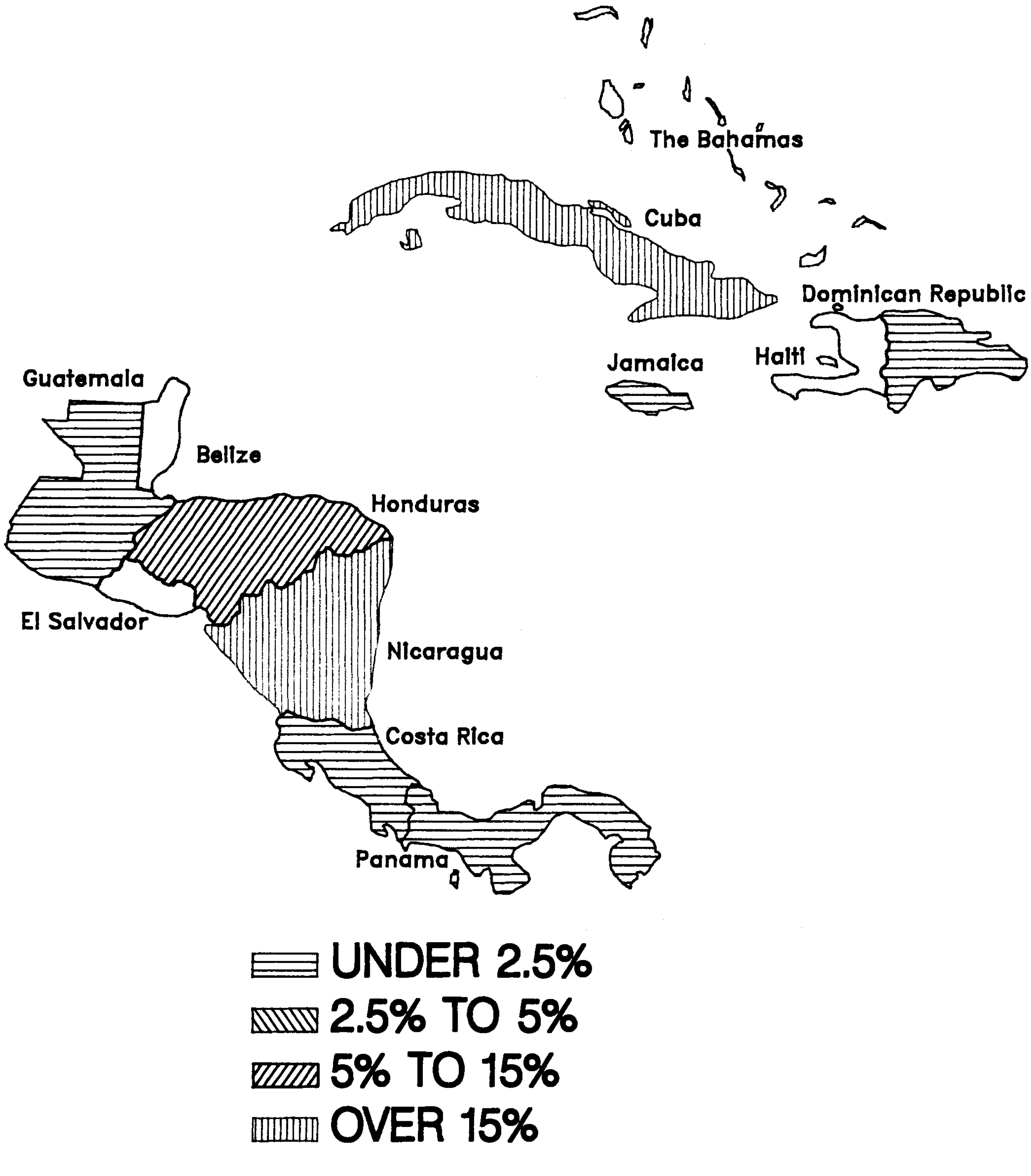
MILITARY IMPORTS AS PERCENT OF TOTAL IMPORTS



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