

THE WORLD BANK GROUP ARCHIVES

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Folder Title: President Wolfensohn - Briefing Book for President's Meetings and Events - Correspondence - Letter to James D Wolfensohn [JDW] from David Young - Managing Director of Oxford Analytica Limited - February 20, 1997

Folder ID: 30488129

Series: Meeting and event briefing materials

Dates: 12/24/1996 - 01/23/1997

Subfonds: Records of President James D. Wolfensohn

Fonds: Records of the Office of the President

ISAD Reference Code: WB IBRD/IDA EXC-13-10

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THE WORLD BANK

Washington, D.C.

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The World Bank

1818 H Street NW

Washington DC 20433

Telephone: 202-473-1000

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30488129

R2002-036 Other #: 39 Box #: 186489B

President Wolfensohn - Briefings Books for Presidents Meetings - Briefing Material
Letter to James D Wolfensohn [JDW] from David Young - Managing Director of

Archive Management for the President's Office

Document Log

Reference # : Archive-01528

1288

Edit

Print

A. CLASSIFICATION

☐ Meeting Material
☐ Trips
☐ Speeches

☐ Annual Meetings
☐ Corporate Management
☐ Communications with Staff

☐ Phone Logs
☐ Calendar
☐ Press Clippings/Photos

☐ JDW Transcripts
☐ Social Events
☒ Other

B. SUBJECT: Letter to Mr. Wolfensohn from David R. Young, Managing Director of Oxford Analytica Ltd., dated February 20, 1997 with attached Oxford Analytica Daily Briefs.

DATE: 02/20/97

C. VPU

Corporate

☐ CTR
☐ EXT
☐ LEG
☐ MPS
☐ OED
☐ SEC/Board
☐ TRE

Regional

☐ AFR
☐ EAP
☐ ECA
☐ LAC
☐ MNA
☐ SAS

Central

☐ CFS
☐ DEC
☐ ESD
☐ FPD
☐ FPR
☐ HRO

Affiliates

☐ GEF
☐ ICSID
☐ IFC
☐ Inspection Panel
☐ Kennedy Center
☐ MIGA

D. EXTERNAL PARTNER

☐ IMF
☐ UN
☐ MDB/Other IO
☐ NGO
☐ Private Sector

☐ Part I
☐ Part II
☐ Other

E. COMMENTS:

File Location

☒ EXC ☐ ISC ☒ Archives

Cleared By

Date:

07/02/97

View Update History

Davos

A L L - I N - 1 N O T E

DATE: 23-Jan-1997 05:26pm

TO: Jane Kirby

(JANE KIRBY)

FROM: Joseph Ingram, EDIDR

(JOSEPH INGRAM)

EXT.: 82046

SUBJECT: RE: Oxford Analytica

Jane,

Have drafted a response to Young's letter for JDW's signature, as per instructions from Ciao. The letter is self explanatory and provides the sort of briefing material you need for him while in Davos. It is not encouraging as to the Bank's ability to help Young directly, though it does hold out hope for possible collaboration with EDI in the future and it does encourage him to attend the Toronto conference where he will have access to potential investors and users of his product. After all, he is a Part I country corporation selling his product commercially -not something we can support directly.

As for Davos, the letter leaves open the possibility that they might bump into one another.

Will send you a copy as soon as Ciao OKs.

Joe

CC: Hany Assaad

(HANY ASSAAD)

CC: VINOD THOMAS

(VINOD THOMAS @A1@WBHQB)

CC: JEAN-FRANCOIS RISCHARD

(JEAN-FRANCOIS RISCHARD @A1@WBHQ)

CC: NIMROD RAPHAELI

(NIMROD RAPHAELI @A1@WBHQB)

CC: JOHN MIDDLETON

(JOHN MIDDLETON @A1@WBHQB)

Davos

A L L - I N - 1 N O T E

DATE: 23-Jan-1997 03:35pm

TO: Joseph Ingram (JOSEPH INGRAM)

FROM: Jane Kirby, EXTVP (JANE KIRBY)

EXT.: 80576

SUBJECT: Oxford Analytica

Joe,

We did meet with JDW mid-day, and he will probably leave the scheduling of a bilateral with David Young of Oxford Analytica to an on-the-spot in Davos.

However, he wants to be briefed on our relationship with Oxford Analytica, any current irons in the fire, and anything he should know.

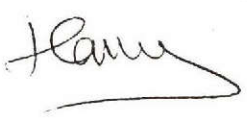
Can you write something up? It can be in an EM form and sent to me or to Hany Assaad.

Thank you,

Jane

CC: Hany Assaad (HANY ASSAAD)

THE WORLD BANK GROUP

ROUTING SLIP		DATE: January 15, 1997	
NAME			ROOM. NO.
Mr. Caio Koch-Weser			D10-095
☐	URGENT	☐	PER YOUR REQUEST
☒	FOR COMMENT	☐	PER OUR CONVERSATION
☐	FOR ACTION	☐	NOTE AND FILE
☐	FOR APPROVAL/CLEARANCE	☐	FOR INFORMATION
☐	FOR SIGNATURE	☐	PREPARE REPLY
☐	NOTE AND CIRCULATE	☐	NOTE AND RETURN
☐		☐	
RE: Mr. Young's letter to Mr. Wolfensohn dated December 24, 1996 "Getting Oxford Analytica Daily Brief Services into selected developing countries"			
REMARKS: Caio: JDW would greatly appreciate knowing how he should reply to the attached. Best regards.  <i>only send copy of the letter. Keep me the report Hany</i>			
FROM Hany Assaad		ROOM NO. E12-31	EXTENSION 30524



cc. Chw
V. Thomas

24 December 1996

14737

James D Wolfensohn
President
The World Bank
1818 H Street N.W.
Washington D.C. 20433
USA

Caio
How moved!
nyph
h

Dear Jim,

Following up on your request in September you may be aware that we last week made a presentation to your colleagues on our proposal to get **Oxford Analytica Daily Brief** services into selected developing countries - to strengthen their "Strategic Information and Analysis Capacity".

Caio did an excellent job of organising everything and we had a good level and receptive audience. For the record, I enclose a copy of the slides we used -- which give all the necessary details. In sum, we have an immediate, concrete and inexpensive way to demonstrate your commitment to using Information Technology to narrow the "knowledge gap" between rich and poor. Moreover it gives you a specific way to demonstrate what you mean by the Banks becoming a 'Knowledge Institution' - trading in intellectual capital - not just monetary capital.

As for next steps - we do fulfil that we would very much like to get three or four pilots off the ground in the next few months. The most promising are Ghana, Bolivia, Jordan and the Philippines through IDF, Infodev or EDI. After that we hope countries will start putting it into their own Bank loan programs.

So if you have occasion to push these along - please do.

Yours sincerely,

David R. Young
Managing Director

PS Hope I can see you briefly in the next few months in order to keep this on track.

DRY/ch

**Oxford
Analytica
Ltd.**

5 Alfred Street
Oxford OX1 4EH, England
Registered office at the above address

Telephone:
Oxford (44-1865) 261600

Fax:
(44-1865) 242018 or
(44-1865) 261626

E-Mail: oa@oxford-analytica.com
Telecom Gold Mailbox No 87-W00666

Registered in England: No. 1196703
VAT No. GB 533 1281 76



**Oxford
Analytica**

Knowledge Partnership

The World Bank
Oxford Analytica

Oxford Analytica



- Why are we here?
- What do we propose?
- What is the relevance to the *Bank Group*?

Why are we here?



- Because we share the goals and vision of the *Bank* ▲
- Because working together will reduce costs for both organizations and improves results
- Because *Oxford Analytica's* core competence, honed over the past twenty years, is well-suited and can make an important contribution



<Link to OADB



What do we propose?

- Under the Rubric of a Knowledge Partnership we propose three concrete and mutually reinforcing ways that *Oxford Analytica* can support the *World Bank Group* in the pursuit of its goals and vision

President Wolfensohn



- **“I want to focus on a specific form of partnership that will take on special importance as we enter the new millennium - a partnership for creating and sharing knowledge, and making it a major driver of development”**

1996 Annual Meeting



Three Programs over the next 18 months



SIAC

Strategic Information and Analysis Capacity



OxWeb

Integrated Information Management

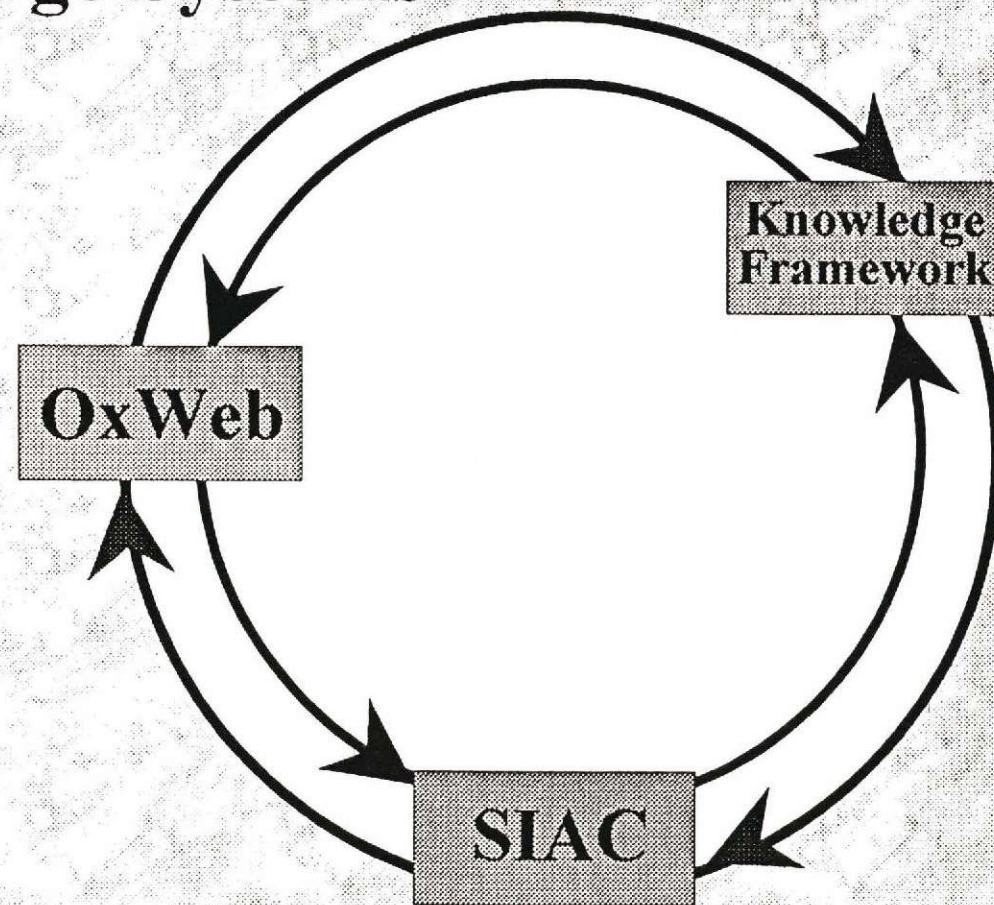


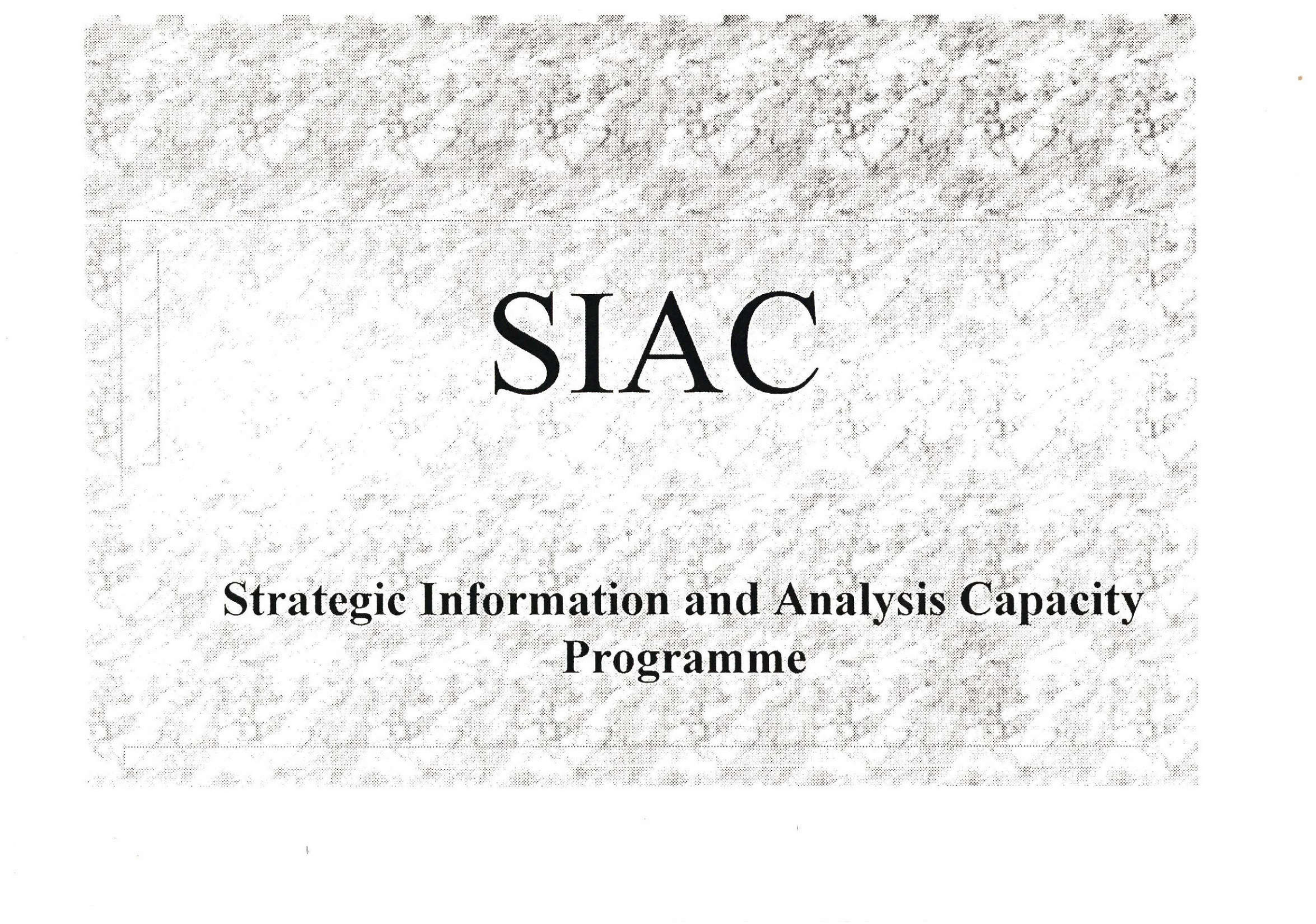
Global Knowledge Framework

Enhanced Open Systems

Mutually Reinforcing

Knowledge Systems





SIAC

**Strategic Information and Analysis Capacity
Programme**

SIAC Objectives



*In support of Accelerated Growth and the
Reduction of Poverty...*

- **Reduce the Information and Analysis Gap
Between Developed and Developing
Countries**



SIAC Objectives (cont.)

■ Improve Public Sector Management and Policy Formulation

- better access to information and analysis
- better quality information and analysis
- improved opportunities for interaction

■ Build Institutional Capacity

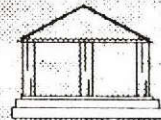
- sustained information and analysis training for senior officials and their staff
- provision of industry standard computer and communication hardware and software
- sustained technology skills training

Plan of Action

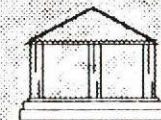
Focus on Key Institutions



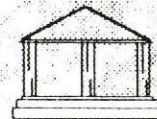
Core SIAC Group



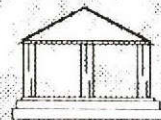
Parliament



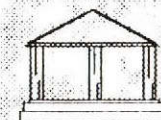
Finance



Executive



Foreign Affairs



NGO
Local Support Group

En. 11/12
P. 10/12
10/12

Three Integrated Components of SIAC:



1) Skills Transfer ▲

2) Installation of Proven Technology ▲

3) Informational Content ▲

SIAC Outputs/Results



- **5 Institutions** will obtain greatly enhanced and sustainable access to timely information and analysis regarding global economic, political and social developments
- Up to **250 institutional personnel trained** in hands-on skills/analysis/policy training courses
- Up to **15 Senior Officials trained** regarding the management of analysis teams, comparative international information strategies and policy, source critiquing methods...+ practical skills
- Support for a **National Information Workshop** /Conference
- International Training/Networking - **8 delegate places** (4 per year) at two international (UK) conferences/working sessions regarding global, regional and national private and public sector issues

SIAC Pilot Projects



■ Pilot locations selected on the basis of their performance, need and ownership

■ Ten Proposed Pilot Locations:

Ghana

Peru

Uganda

Romania

Philippines

Poland

Benin

Palestinian Authority

Bolivia

Jordan

Ownership in Ghana



■ **“We view the SIAC Project as a priority in Ghana’s efforts to achieve middle income status, and would appreciate all the support you can give for the speedy implementation on the ground...”**

- **Kofi Totobi Quakyi**
- **Minister of Information**
- **in Letter to World Bank Res. Rep.**
- **August 1996**



Cost and Finance of SIAC Pilots



- USD\$300,000 in each of two years per SIAC Project
- Co-financed by the *World Bank*, the *Oxford Analytica Trust* and the Client Government
- Post-project running costs decrease dramatically and are easily adjusted by client to a sustainable level

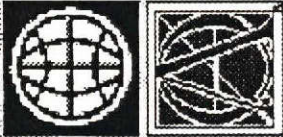
World Bank Group Support



- **Institutional Development Fund**
- **InfoDev**
- **Economic Development Institute**
- **Loan Programmes**

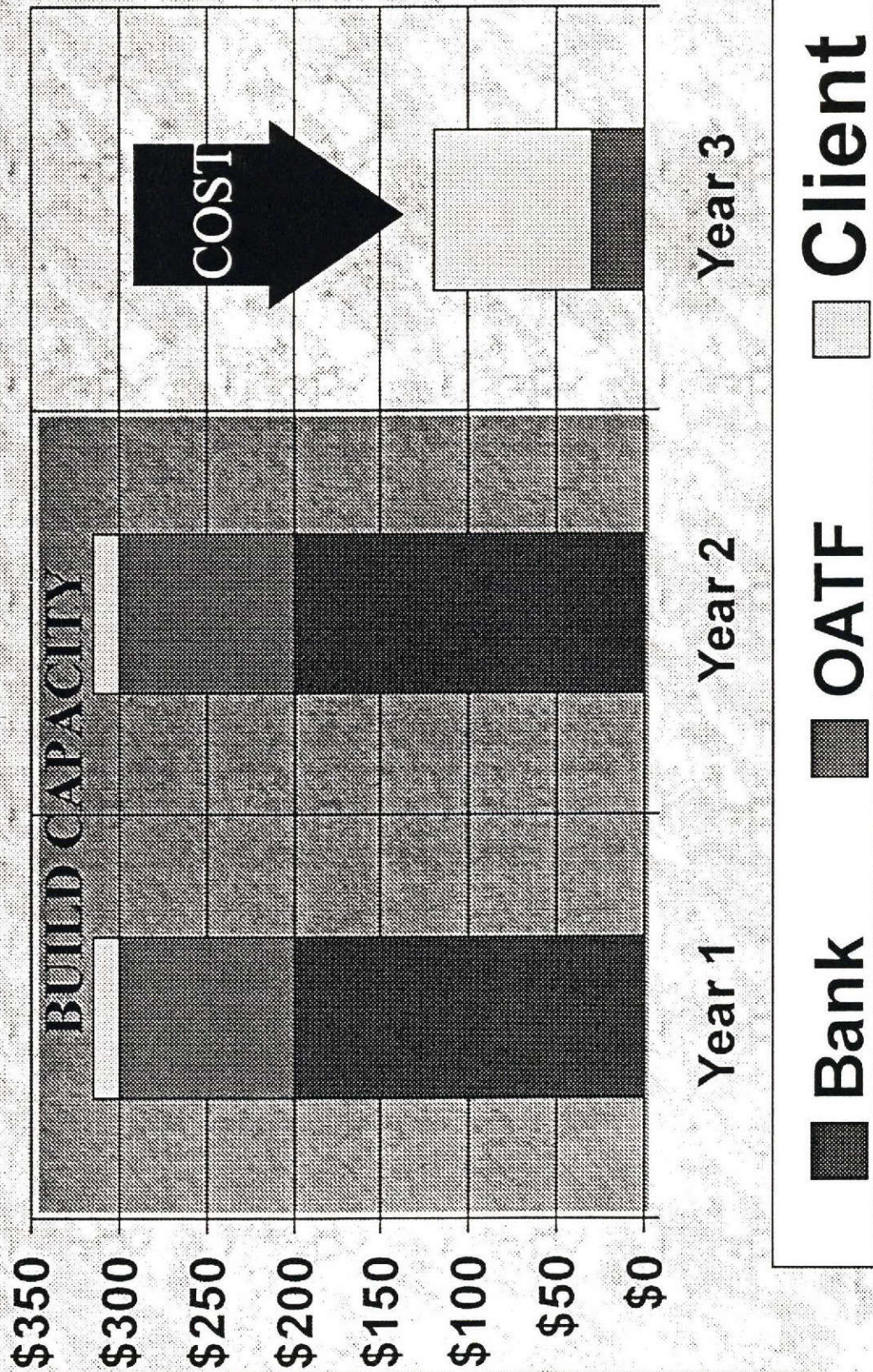
"We need to invest in the necessary systems, in Washington and worldwide, that will enhance our ability to gather development information and experience, and share it with our clients. We need to become, in effect, the Knowledge Bank" -- J.D. Wolfensohn 1996





SIAC Costs and Funding Structure

USDS(1000s)



Benefits of SIAC



- **Concrete Action Now (support teams ready)**
- **Builds Upstream Capacity ▲**
- **Complements other Bank Projects**
- **Catalyst for Development of “Global Knowledge Framework”**
- **Uniquely Sustainable and Economical**

Moving SIAC Ahead...Next Steps



- Country Selection and Ownership ▲
- Collaborate with *Bank* Country Team
- Finance SIAC Pilot Projects ▲
- Begin Implementation

OxWeb

Integrated Information Management

OxWeb = Content + Management



Features:

- Daily Alerts and Analysis ▲
- Profiling to Meet Individual Interests
- Uses the Internet and Intranets-- Easily Integrated with Other Systems
- Channel to Complementary Information
- Continually Adding Value

Network Information Management Tool



- Internet Solution for Client Countries
- Intranet “add-in” for World Bank Group

Demo

[Link to ScreenCam](#)

Global Knowledge

Framework for Enhanced Open Systems



Global Knowledge Framework

- Global Access to the *Bank* as a Knowledge Institution
 - Common Reference Points/Framework
 - Shared Understanding
 - Collaborative Problem Solving--*Bank* & Clients
 - Key to a Broader, More Integrated Approach to Development-- “The New Paradigm”
 - Precursor: 10 SIACS interacting with the *Bank* and each other
- ▲
Global Vision

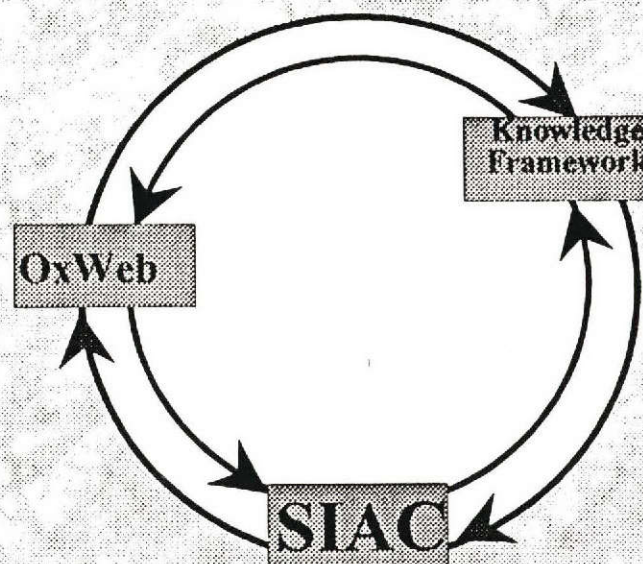
Conclusion

Knowledge Partnership



Knowledge Partnership

Goal Convergence: *Oxford Analytica* and the *World Bank* are working in the same direction. Working together we can lower costs, improve quality and accelerate progress



Our Contribution

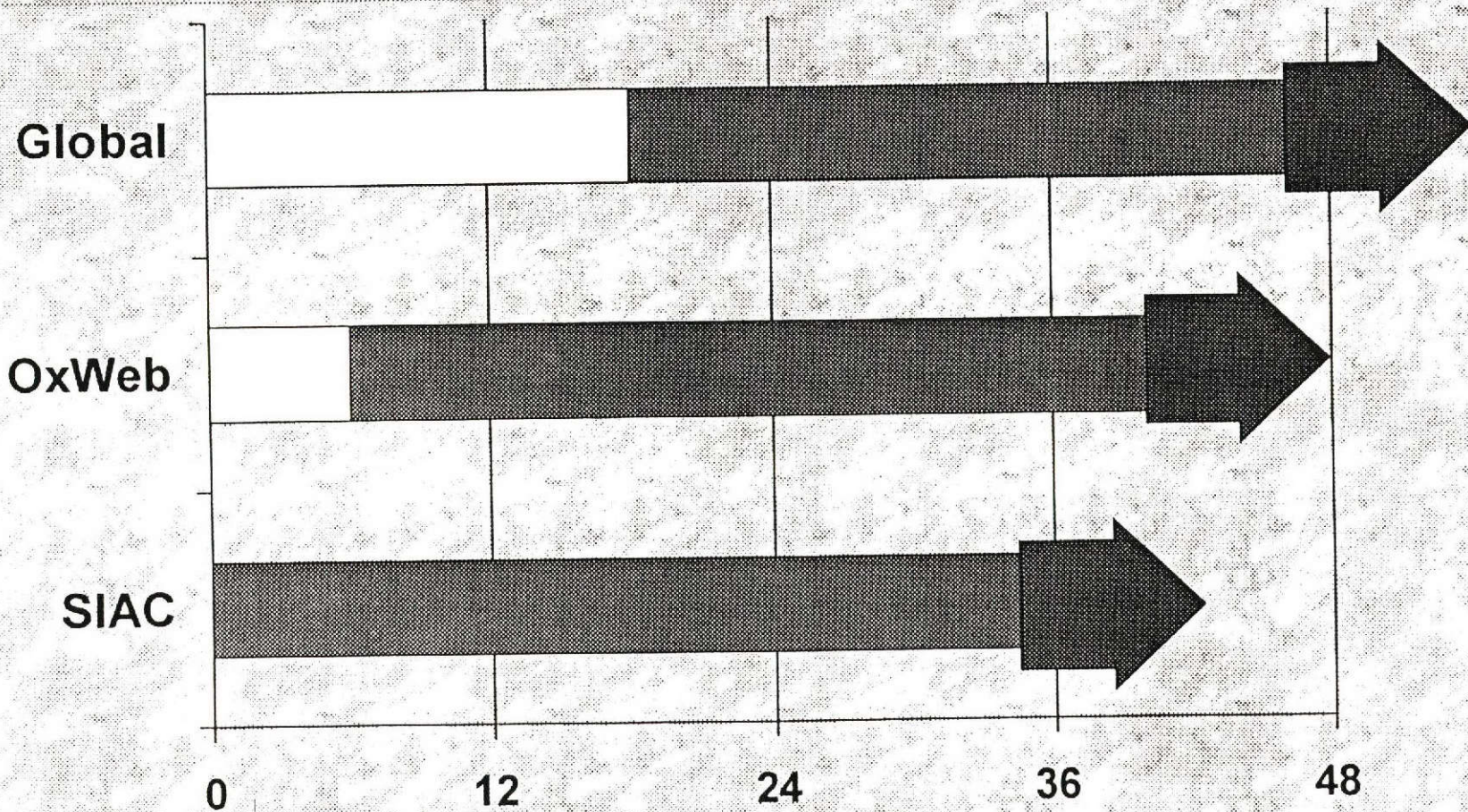


Oxford Analytica is

- Well known to the *Bank*
- Experienced in the timely production and global distribution of action-oriented information and analysis
- Abreast of relevant technologies
- Traditionally strong in education and training
- Prepared to co-finance and implement concrete projects immediately

Timing

(in months from Jan. 1997)

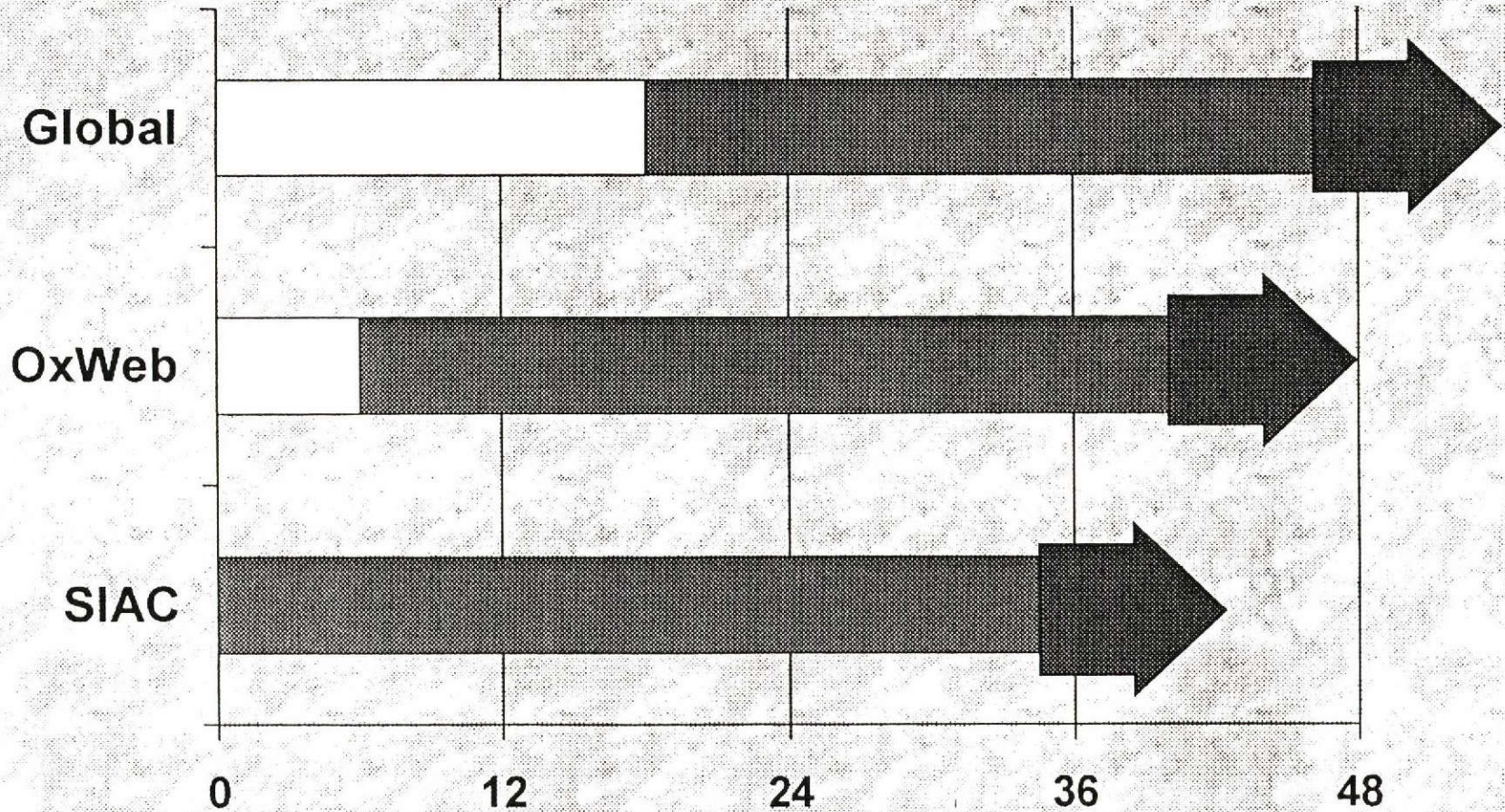




Thank You

Timing

(in months from Jan. 1997)



Slide Links

Referenced from main body



Products and Services

Oxford Analytica's products and services fall into three categories.

- Research and Consulting
- Conferences, Briefings and Seminars
- *Oxford Analytica* Daily Brief Services ▲

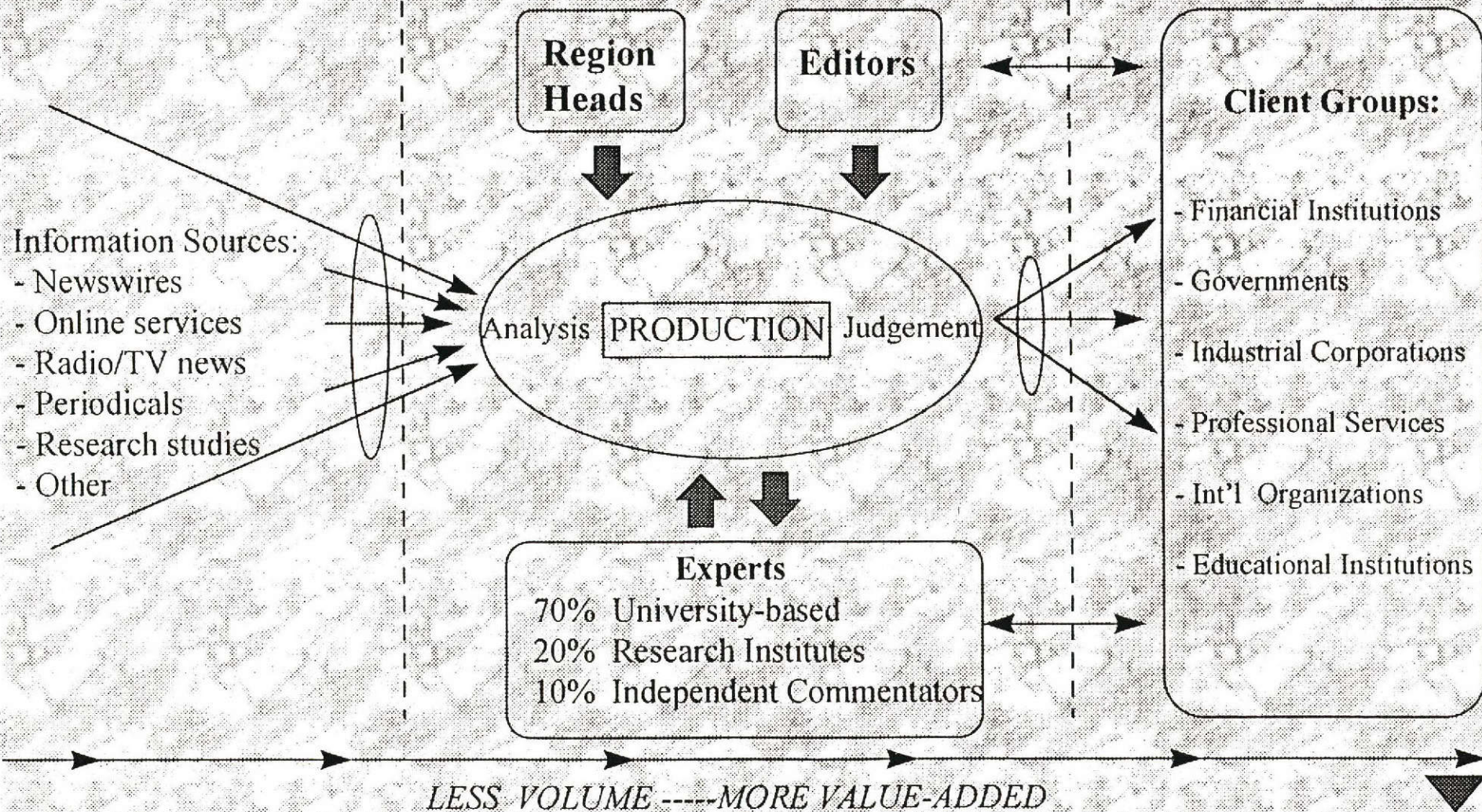
Oxford Analytica Daily Brief

Process

Information Collection

Core Process

Client Relationships





Shared Goals and Vision

in Developing Countries...

- Build Capacity
- Accelerate Growth
- Harness Information Technology for Development

in the *World Bank*...

- Develop Knowledge Systems for Enhanced Internal Efficiency and Client Support



Quote





SIAC Training and Support

- **Unique On-line Training and Support**
 - Technology AND Analysis Training
 - WWW and Email allows continuous interaction, monitoring and evaluation
 - Support materials for self-paced, practical courses
- **On-site Workshops and Seminars**
 - Separate courses for high-level officials and their staff
- **Education Tools - *Global Vision* Multimedia Database (CD)**





Proven Technology

- 3-5 PCs in each of 5 Participating Institutions
- Internet Access (email and WWW)
- Fully Integrated Software (using industry standard and/or open specifications)
- Databases installed on-site and updated using the Internet ▼

Open Access to Information



Via the Internet (WWW and Email)...

- *Oxford Analytica's* Daily Brief Services
- *World Bank Group's* Knowledge Base (i.e. "Knowledge Institution")
- All Relevant Sources Around the World





Benefits of Open Access

- Clients Better Informed
- Reduces Client's Isolation - "Window to the World"
- Clients have Increased Opportunities for Comparison, Interaction, and Model Building --Researching, Learning and Disseminating the Lessons of Development
- Raises Client's Awareness of Outside Perspectives



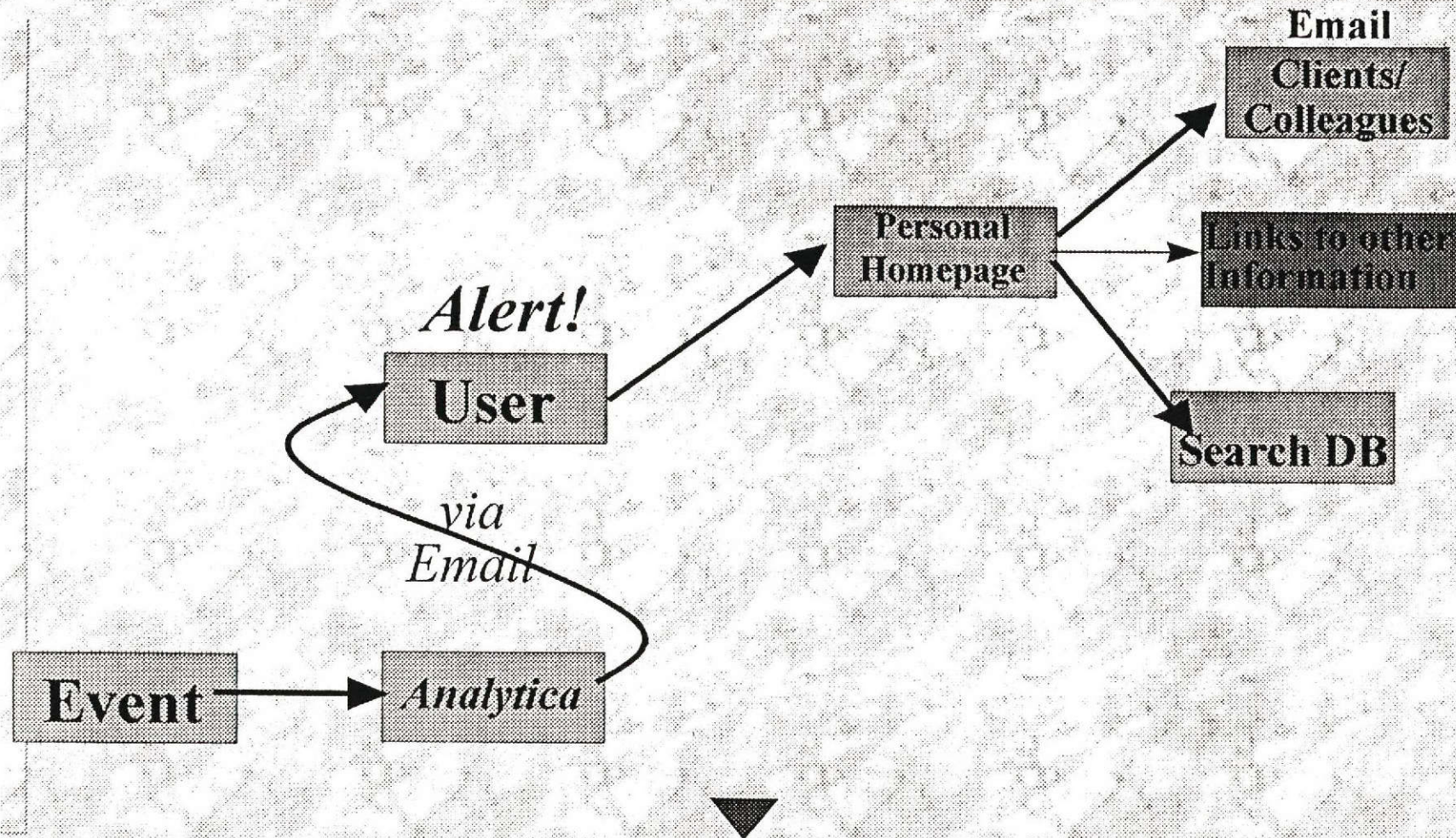


Upstream Capacity

- Strengthens key institutions by building essential skills and technology base
- Will help key policy makers understand information technology and related issues--important for their building of their national information infrastructure



OxWeb Alert Process



Oxford Analytica

Daily Brief®

January 31, 1997

I

UNITED STATES: Trade Fast-Track

EVENT: Acting USTR Charlene Barshefsky indicated yesterday that the Clinton administration has not yet decided on the scope of 'fast-track' authority it will seek from Congress.

SIGNIFICANCE: Barshefsky has pledged to work with Congress to agree on a formula for fast-track negotiating authority. However, with the two branches deeply divided, any simple resolution looks highly unlikely in the short term.

ANALYSIS: Discussions over the scope of 'fast-track' authority held between the White House and leaders in the House of Representatives broke down in 1995, thus stalling negotiations to incorporate Chile into NAFTA (see OADB, September 20, 1995, II). Fast-track authority has been used in the approval process for many recent trade agreements, including both the Tokyo and Uruguay Round GATT accords, the US-Canada Free Trade Agreement and NAFTA. It provides for congressional consideration of such trade agreements by a simple 'yes or no' vote in Congress, without the possibility for amendment, and is now regarded as a necessary condition to prevent Congress from unravelling complex trade accords.

At her confirmation hearings yesterday, Charlene Barshefsky -- whose nomination as permanent US trade representative was yesterday unanimously approved by the Senate Finance Committee, and is likely to be voted on by the full Senate next week -- indicated the administration has yet to decide on the scope of the fast-track authority it will seek from Congress. It is considering whether to seek limited authority to extend NAFTA to include Chile or to ask for more general authority, enabling it to negotiate either a western hemisphere free trade agreement or even more generally on any trade issues.

Chilean NAFTA bid. On his visit to Washington next month, Chilean President Eduardo Frei is expected to reiterate Santiago's desire to join NAFTA. In addition, he will discuss further efforts to increase trade and investment. Chile is reluctant to allow NAFTA negotiations to proceed without a fast-track commitment from the Clinton administration; the breakdown of earlier talks is regarded as an embarrassment by both parties.

Further ahead, the annual meeting to discuss progress on achieving the Free Trade Area of the Americas (FTAA) will be conducted in May with the potential members. In December 1994, the Clinton administration pledged during the Miami summit to inaugurate the hemispheric-wide FTAA by 2005. Although little progress was expected between the summit and last year's presidential election, the administration will need to outline a firm position soon if it is to meet the 2005 deadline for establishing the area.

Congress-administration differences. In its first term, the Clinton administration's position was to seek fast-track authority applicable not only to primary trade issues, but also to negotiation of side-accords covering environmental and labour concerns. Both these issues are important to significant Democratic constituencies. However, in contrast with NAFTA negotiations, the relatively small size of the Chilean economy has meant that no influential business constituency pressing for rapid



OXFORD ANALYTICA EXECUTIVE BRIEF

13.00 GMT, Friday, January 31, 1997

FRANCE: Figures released today show an unexpected 29,000 fall in the number of unemployed in December. The overall rate remained at 12.7%. The government will welcome the decrease as a further sign of economic recovery. Officials warned, however, that changes in the registration method may have distorted the figures. Lower unemployment is critical to the government's political fortunes, but the overall trend remains upward. **Brief forthcoming.**

***UNITED STATES:** The administration's present trade fast-track priorities do not appear to be reconcilable with Republican views. Accordingly, any fast-track authority granted is likely to be narrowly defined in both scope and duration. **See OADB today.**

William Daley was yesterday confirmed by the Senate as commerce secretary, while Charlene Barshefsky's nomination as permanent trade representative was approved by the Senate Finance Committee. The Senate Intelligence Committee delayed hearings on CIA Director-designate Anthony Lake, pending release of an investigation into his equity dealings. The smooth confirmation thus far of President Bill Clinton's appointees suggests that Republicans will intensify their scrutiny of Lake. Even if he secures approval, Lake will begin his tenure significantly weakened. **See OADB, December 6, 1996, I.**

***TURKEY:** Falling interest rates and expectation of an drop in inflation have fuelled an upwards surge in the Istanbul stock market index. The rise is likely to continue, although not at its present rapid pace, with intermittent corrections. **See OADB today.**

***CIS:** Moscow increasingly is seeking to develop integration and cooperation within the CIS in defence-related fields. In spite of some progress, however, its ambitions are unlikely to succeed. Instead, they are likely to prove a source of tensions within the CIS. **See OADB today.**

SOUTH KOREA: State prosecutors today applied for a warrant to arrest Hanbo group founder Chung Tae-soo in connection with the company's collapse. The affair highlights the twin problems of corporate indebtedness and bank over-exposure. To minimise future recession-induced collapses, major industrial and banking restructuring may be necessary. **Brief forthcoming.**

***INDIA:** Political consensus on infrastructure development should result in the implementation of many of the recommendations contained within a report on infrastructure commercialisation, recently submitted to the government. However, future infrastructure funding depends to a great extent on implementing measures to improve the debt market. **See OADB today.**

INTERNATIONAL: Institute of International Finance figures released yesterday show capital flows to emerging markets reached a record 231.5 billion dollars in 1996. Flows are expected to plateau this year. Although equity investment flows have risen in recent years, the susceptibility of flows to changes in industrial country interest rates remains a risk, as does the build-up of short-term debt in some countries. **See OADB, September 24, 1996, IV.**

***IRELAND:** The government's expansionary budget is designed to reverse its opinion poll deficit in the approach to this year's general election. If the government regains the initiative domestically, and if it can avoid further political pitfalls, the growing economy, lower taxes and industrial peace provide a solid basis for an election victory this year. **See OADB today.**



THE OXFORD ANALYTICA DAILY BRIEF®

January 31, 1997

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 - II Turkey: Stock Market Rally
 - III CIS: Military Integration
 - IV India: Infrastructure Funding
 - V Ireland: Election Economics
-

INDEX OF RECENT COVERAGE

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- II United States: Medicare Politics
- III East Asia: Security Balance
- IV Israel: Privatisation Plans
- V International: Land Mines

January 29, 1997

- I Afghanistan: Talibaa Thrust
- II International: Defence Industry
- III United States: HMO Profitability
- IV Croatia: Election Economics

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action to free US-Chilean trade has emerged. In 1995, Chilean exports to the United States were approximately 2.4 billion dollars; US exports to Chile were about 3.8 billion. Given the lack of such pressure, it has been speculated that Mickey Kantor, then USTR, allowed the 1995 fast-track negotiations to collapse because the administration did not want to engage in any politically controversial trade negotiations in the run-up to the 1996 presidential election.

Although this motivation no longer hinders administration action, serious substantive differences remain between White House and congressional positions:

1. Republicans object to applying fast-track to labour and environmental issues because:
 - they disagree with the general principle of conducting such negotiations under terms that present an agreement for congressional consideration without allowing for the possibility for amendment; and
 - they believe such issues are appropriately considered as international treaties, rather than as trade agreements.

When an international treaty comes before the Senate for its advice and consent, a two-thirds majority is required for approval, rather than the simple majority that applies to trade agreements. Republicans, many of whom oppose the substance of labour and environmental accords, argue that extending fast-track to such issues diminishes the Senate's historic constitutional role.

2. Congress remains reluctant to extend fast-track authority to apply to trade issues only on the grounds that the administration abused that process and pushed through provisions with minimal trade significance as part of the Uruguay Round approval legislation. Critics point to provisions applying to pensions guaranteed by the federal government and the requirement that businesses file their taxes by wire rather than by cheque as examples of such abuse.

Narrow authority possible. Republican Senator Phil Gramm introduced two separate bills last week to grant fast-track authority, despite his party's concerns. One bill applies specifically to Chilean NAFTA accession negotiations, with Gramm arguing that such discussions -- which optimists have suggested could be concluded in 60 days -- should not be held hostage to more general trade liberalisation efforts. The second Gramm proposal would allow permanent fast-track authority to negotiate a FTAA (exclusive of Cuba, in the absence of 'constitutionally guaranteed democratic government' established 'with leaders chosen through free and fair elections').

Both Gramm bills would explicitly prohibit applying fast-track to trade and environmental issues. They would also make it possible to challenge extraneous provisions not deemed necessary to implementing the trade agreement on a point of order, and if sustained, allow for the extraneous provision to be struck from the bill (rather than cause the entire bill to fail). A similar rule currently applies to Senate consideration of extraneous provisions in budget reconciliation bills.

At present, a wide gulf exists between the administration position and the more circumscribed Republican stance on environmental and trade issues. Clinton will find it hard to accept limited fast-track authority without offending important Democratic labour and environmental constituencies. At the same time, Republicans are reluctant to consider fast-track without a clear statement from the president explaining why fast-track authority is necessary and a commitment to secure his party's support for electorally unpalatable trade initiatives.

It is not clear that either Congress or the administration wishes to make further trade liberalisation a high priority at this time (see OADB, November 19, 1996, I), especially in the face of evidence suggesting that NAFTA's benefits were oversold and its costs underestimated. Thus, any grant of fast-track authority will probably be quite limited. Whilst compromise on narrow authority to enter



into discussions with Chile may be achieved, more sweeping authority to liberalise trade on a hemisphere-wide basis is unlikely in the short term.

CONCLUSION: At present, administration fast-track priorities do not appear to be reconcilable with Republican views on trade issues. Accordingly, any fast-track authority granted is likely to be narrowly defined in both scope and duration.

Keywords: NA, United States, Chile, NAFTA, economy, politics, trade, policy, integration, legislation, party, government



Oxford Analytica

Daily Brief®

January 31, 1997

II

TURKEY: Stock Market Rally

EVENT: The Istanbul Stock Exchange's leading index has jumped over 50% in dollar terms since the beginning of the year.

SIGNIFICANCE: The upwards trend has been fuelled by falling interest rates and expectations of a drop in inflation this year. The go-ahead for privatising Turk Telekom has added further impetus to the rise.

ANALYSIS: The Istanbul Stock Market's National-100 index yesterday closed at 1,643 points, up from 995 at the beginning of 1997. This represents a rise of 68.4% from end-1996, and a gain of 54.2% in dollar terms. It follows the 143.8% overall rise in the index last year (a gain of 35.8% in dollar terms). The daily volume of trading has also soared this month. It hit a record 71.9 trillion lira (626 million dollars) on January 28, compared with a daily average of 152 million dollars in 1996.

The market's rise this year has been triggered in part by falling interest rates. Compounded annually, rates on Treasury bills sold at auction have dropped to around 86.5%, after peaking at about 126% in late November. Expectations that rates will continue a downwards trend have contributed to the rising liquidity in the equities market.

The quiet currency market has further encouraged investors to turn to equities. The lira depreciated 3.4% against a dollar-DM currency basket. This rate is roughly in line with monthly inflation expectations. Indeed, these expectations themselves have contributed to positive market sentiment. The lower-than-expected increase in wholesale price index inflation, which rose 3.9% in December, was perceived as evidence of slowing inflation. The annual figure is expected to fall to about 65-70% this year, down from 84.9% in 1996.

Telecom privatisation. The market rally has gained particular momentum since January 23, when the Constitutional Court rejected a challenge to legislation permitting the privatisation of Turk Telekom, a centrepiece of the Islamist-led government's sell-off plans for 1997. The privatisation administration is expected to begin with the sale of 34% of the state's share in the telecoms company (the government has already included 3.2 billion dollars in revenues from the sell-off in its 1997 budget calculations). These revenues represent about 74% of the government's total privatisation target for this year. The sale of Turk Telekom is due to be completed in 1998.

The Constitutional Court's decision is perceived by many analysts as evidence that the government could speed up the privatisation of other state-owned enterprises. In addition to the telecoms company, the government has slated steel-maker Ereğli, the oil refinery Tupras and the petroleum distributor Petrol Ofisi for privatisation this year. Since 1985, this government's programme has generated a mere 3.1 billion dollars in state revenue, and financial circles have pushed successive administrations to accelerate the sell-off programme as a means of controlling Turkey's spiralling domestic debt burden. Revenues from privatisation could enable the government to finance debt payments without having to resort to Treasury auctions.



Market outlook. In spite of its upwards trend, the market has shown a degree of short-term volatility. The court ruling triggered an immediate three-day burst, during which the National-100 index gained 36%, closing at 1,700 on January 27. In dollar terms, the index rose 26% over this period. Demand for equities centred on utilities and companies slated for privatisation: Eregli shares alone accounted for 11% of the total volume of trading on January 24.

However, the index dropped by 8.7% on January 28 -- the day trading volumes hit a record level -- amid heavy profit-taking. The correction was triggered in part by doubts about whether Eregli's sell-off would indeed go ahead this year after the privatisation administration announced that only two bids were received for the company tender. The rise resumed the next day in response to news that the privatisation administration may handle the sale via a convertible bond issue.

Barring unforeseen negative political developments, signs that inflation will remain low compared with last year and that the government is making progress on structural reforms should sustain the index's upward trend. The privatisation administration sold about 900 million dollars' worth of state assets in January, compared with just 290 million in the whole of 1996. In a further indication of its commitment to reform, the government is discussing a restructuring of the bankrupt social security system.

CONCLUSION: The upward trend in the market should continue, although not at its present rapid pace, and daily trading volumes will remain high as long as equities offer higher yields than any alternative investment vehicle. Nevertheless, corrections will take place intermittently.

Keywords: ME/NAF, Turkey, economy, industry, equities, privatisation, telecommunications



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III

CIS: Military Integration

EVENT: Russian CIS Cooperation Minister Aman Tuleyev suggested this week that the CIS could become the basis of a new military bloc.

SIGNIFICANCE: Moscow increasingly is seeking to develop integration and cooperation within the CIS in defence-related fields.

ANALYSIS: The formal basis for close CIS military ties has been in place since the 1992 Collective Security Treaty, which links Russia with Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Tajikistan and Uzbekistan. In addition, there are over 240 bilateral, multilateral and common defence treaties and agreements signed within the CIS on various aspects of defence-related cooperation.

Although Moscow's effort to promote military links with other CIS states is long-standing, it is now receiving greater priority and being pursued with greater vigour, for a wide variety of reasons:

1. **Defence considerations.** Russian Defence Minister Igor Rodionov is aware that greater CIS cooperation could help to overcome some of the problems facing the Russian military, from providing comprehensive air defence cover to creating large enough defence orders to support research and development programmes. For example, it is clear that Russian orders and projected export sales alone will not support the development of new air superiority fighters or precision-guided missiles.

2. **Rodionov reform drive.** Following his purge of conservatives within the High Command (see OADB, October 31, 1996, I), Rodionov has looked to officers from the CIS Joint Staff as a source of allies in his efforts to implement serious military reform. Russian Chief of the General Staff Colonel-General Viktor Samsonov is the most prominent of these, as former chief of the CIS Joint Staff; Major-General Gennadii Zolotukhin, head of administrative affairs at the defence ministry (MO), and General Staff Coordination Chief Lieutenant-General Leonid Ivashov are also from the CIS Staff, as is Colonel-General Leonid Maierov, now deputy secretary of the Security Council. Samsonov has urged a much greater role for the CIS in Russian military planning.

3. **NATO enlargement.** The prospect of NATO's eastwards enlargement has encouraged Moscow to look for counter-balancing alliances, whether as genuine defensive structures, or as face-saving gestures and moves aimed at nationalists in the Duma.

4. **Regional stability.** There are genuine threats to regional stability -- especially in Central Asia -- which are difficult or impossible to solve or check on a national level. For example, the civil war in Tajikistan is regarded as a conflict which Russia cannot allow itself to abandon. The Taliban's success in Afghanistan (see OADB, January 29, 1997, I) has sharpened such concerns.



5. Foreign links. Moscow is increasingly concerned about what it sees as the penetration of the CIS by rival powers, especially the United States in Uzbekistan, Turkey in the Transcaucasus and Iran in Central Asia. In part, such foreign links are visible in defence relations. For example, Turkish and Iranian officers have been involved in training Azerbaijani troops, and the United States has an increasingly strong cooperation programme with Uzbekistan's army. Although the MO does not yet regard such involvement as a direct threat, it has been encouraged by other agencies -- notably the foreign ministry's CIS Department, the Ministry for CIS Cooperation and the Foreign Intelligence Service -- to foster renewed military ties within the CIS in order to exclude such outside influences.

Russian aims. The best CIS cooperation so far is probably to be found in the field of intelligence and border control. CIS Border Troop commanders meet regularly under the chairmanship of General Andrei Nikolaev, commander of Russian border troops. A draft 'Agreement on Cooperation in the Event of Crises on External Borders' was agreed at the commanders' last meeting in December, with only Uzbekistan absent.

Although Russian CIS Cooperation Minister Aman Tuleyev's suggestion on January 27 of a single military bloc is premature, the Russian High Command has identified three specific priorities:

1. Invigoration of the CIS Joint Staff. This is to take place under continued Russian command. Russians have dominated the Staff from the first and, despite its recent failure to dictate Samsonov's successor as chief of the Joint Staff, Moscow appears unprepared to concede more than one or two of the three deputy Joint Staff chief posts to non-Russians.

2. Greater cooperation in air defence and border control. In the past few months, General Viktor Prudnikov, commander of Russia's air defence troops, has been trying to extend and raise the profile of work in this field. Russia, Kazakhstan and Belarus already work together and share targeting data, and Armenia and Georgia are set to join their network this year. With longer-term cooperation in view, the Granit financial-industrial group (FPG) is being formed to bring together Armenian, Belarusian, Georgian, Kazakh, Russian and Ukrainian firms to develop a common CIS air defence system.

3. Common CIS military doctrines, tactics, training and equipment. This would not only facilitate joint operations but also assist Russian arms exports. This is one reason why both the Military-Industrial Commission and the Ministry for Foreign Economic Relations have supported this aspect of the MO's plans.

Integration prospects. Moscow sees such measures as constituting, ideally, steps towards the goal of comprehensive CIS military integration. However, it is increasingly focusing its efforts -- as in several non-military fields -- on specific, practical forms of cooperation within the grouping.

This is because many other CIS states are beginning to raise serious doubts about the value of military integration, and even cooperation, within the CIS. Ukraine has long opposed any developments which might allow Russia to use the CIS as a tool of regional hegemony; but Uzbekistan has also begun to block many of Moscow's initiatives, as it seeks to assert itself as Washington's Central Asian favourite and principal regional rival of the more pro-Moscow Kazakhstan (see OADB, January 14, 1997, IV). For example, in November, Tashkent orchestrated the rejection of Moscow's proposal that former Russian chief of staff General Mikhail Kolesnikov should succeed Samsonov as chief of the CIS Joint Staff, arguing that the post should go to a non-Russian.

The trend seems to be against integration even within the core of CIS states with which Russia has strong security ties. According to First Deputy Foreign Minister Boris Pastukhov, these are Armenia, Belarus, Georgia, Kazakhstan, Kyrgyzstan and Tajikistan. However, Armenia and Georgia are often



grudging allies, with Tbilisi in particular becoming more assertive (see OADB, January 20, 1997, III); Kyrgyzstan is militarily negligible; and Tajikistan is less an ally than an open-ended military commitment. Belarus is the most enthusiastic proponent of ties with Russia, but the relationship is envisaged as a privileged bilateral one rather than a CIS one, and it falls well short of full military integration. On January 22, Belarusian Defence Minister Lieutenant-General Alyaksandr Chumakow went out of his way to rule out any merger of forces or even joint command systems.

Given Russia's particular defence industry needs and wide-ranging security concerns, there is particular scope in defence-related fields for the development of a variegated network of bilateral and multilateral ties (with the latter including agreements among several, but not all, CIS members). However, progress will be difficult as long as even such less-than-comprehensive links are seen by Moscow -- as they are -- as part of its wider CIS integration agenda. For example, the Granit project may be beneficial for Ukraine's defence industry, but several CIS states will resent and resist Russian efforts to use such FPGs to shape their economic development to fit Russian needs or to facilitate greater political control.

In this context, defence integration looks set to become one of the major fault-lines within the CIS this year. The Russian High Command is neither able nor willing to pull back from its position on the necessity of integration, and, given that crucial progress towards NATO enlargement appears certain this year, a retreat on CIS defence ties would be politically insupportable. Furthermore, unless and until they receive definite government pledges on adequate funds for military reform, Rodionov and Samsonov also see the CIS as a vital stop-gap.

CONCLUSION: Although progress is being made in particular CIS cooperation projects in defence-related fields, Russia's ambitions for comprehensive CIS military integration are unlikely to succeed; rather, they are likely to prove a counter-productive source of tensions within the CIS.

Keywords:EE, CIS, Russia, international relations, politics, security, foreign policy, defence, military



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IV

INDIA: Infrastructure Funding

EVENT: An expert group recently submitted its report on the commercialisation of infrastructure.

SIGNIFICANCE: The report's recommendations will have a significant influence on government initiatives regarding the development of the country's infrastructure.

ANALYSIS: A group of experts, set up by former finance minister Manmohan Singh in October 1994, recently submitted its report to government on the commercialisation of infrastructure. The group -- which included representatives from financial institutions, stock exchanges, senior government officials and corporate managers -- was headed by Rakesh Mohan, the director-general of the National Council of Applied Economic Research and a key author of the industrial policy followed by India since 1991.

According to the report, India's infrastructure investment needs to rise from the current level of 5.5% of GDP to 7% in fiscal 2000-01, and to 8% after a further five years. In absolute terms, the annual investment in infrastructure should rise from the current 17 billion dollars to 30 billion in 2000-01, and to 50 billion by 2005-06. As such, it is estimated that 15 billion dollars will need to be invested in infrastructure over the next five years. Given the constraints on government expenditure for the foreseeable future, much of this money will have to come from private sources.

Funding and debt market reform. The net flow of foreign capital is projected to rise from the current level of 7 billion-8 billion dollars to about 17 billion-20 billion in 2000-01. However, while the government is keen to attract foreign capital to help fund infrastructure development (see OADB, June 13, 1996, III), it is pessimistic about official debt flows. The report estimated that although 30-35% of the total external capital flows would go towards infrastructure financing, this would meet only 15% of the total requirement. The remaining 85% would have to be financed domestically, with possibly 40% being provided by the capital market.

The final 45% of funds would have to be raised through the debt market. To improve the mechanism between savers and borrowers, the report recommended various reforms, including:

- allowing domestic and foreign private insurance companies, and new private and public pension funds to participate in the market;
- introducing tax benefits for investments in infrastructure projects;
- allowing private sector companies to issue tax-free bonds; and
- developing a municipal bond market.

A further measure recommended in the report which would allow foreign institutional investors (FIIs) to participate in the debt market has already been adopted. The Securities and Exchange



Board of India yesterday announced that foreign investment institutions will be permitted to set up mutual funds to invest in Indian debt instruments.

The report also emphasised the need for government support for private projects, and suggested that the state should take significant equity positions in infrastructure projects in order to help attract commercial equity and debt. Once viable, the government could then transfer its support to new projects.

Regulatory frameworks. The government was also encouraged to create a transparent framework to facilitate negotiations on build-operate-transfer (BOT) projects and simplify the regulatory framework governing private infrastructure projects. The report specifically recommended that:

- government agencies should not combine the roles of regulator and operator;
- autonomous regulatory bodies should be established;
- all sector-specific enactments be unified in a single statute;
- mechanisms to settle disputes quickly must be set up;
- a body similar to the Foreign Investment Promotion Board be set up to clear proposals for infrastructure projects; and
- investment restrictions on FIIs for investment in infrastructure projects be removed.

The report also made recommendations relating to a number of specific sectors:

1. **Urban infrastructure.** The provision of urban services such as water supply and solid waste management should be put on a more commercial basis. As such, solid waste disposal should be completely privatised, along with water sourcing, treatment and bulk supply, while water distribution and pricing should remain in the public sector.

2. **Power.** The state electricity boards (SEB) should be restructured, to avoid the same units combining the functions of generation, transmission and distribution. The SEBs are running at heavy losses because they have to supply power to farmers at subsidised prices. The report suggests measures to phase in cost-based pricing for each consumer. It also recommends the setting up of a Central Electricity Regulatory Commission, operating outside the government's control, as a way to smooth negotiations with private companies. It further suggests that the government should determine a benchmark price for energy, and give an unambiguous political mandate that would allow private contractors to secure the target price or break off negotiations.

3. **Telecoms.** It was recommended that long-distance telecom services be opened to the private sector by 2001 and that the telecom licence fees paid by private companies should be used for infrastructure investment. In addition, the report suggested that the state-controlled MTNL company, which provides basic telecom services in Delhi and Bombay, be further privatised, and that the Department of Telecommunications be converted into a commercial entity.

4. **Roads.** Financing road development has been a major concern. As such, the report recommended setting up a Highway Infrastructure Savings Scheme to channel savings into the sector. Substantial portions of revenues from taxes on motor vehicles and fuel should also be earmarked for road development.



5. Industrial parks. Contrary to demands by some foreign investors to obtain land at concessional rates, the report was in favour of selling land for industrial parks at market prices. It also suggested that industrial parks should be treated on par with the power, telecom and road sectors in terms of tax and tariff relief.

6. Ports. The report recommended that port authorities be permitted to raise resources from the primary market and suggested that the Major Port Trust Act of 1963 be amended to permit BOT projects. The report also suggested that a separate regulatory authority should be set up to consider issues relating to pricing and conditions governing private participation in port development.

Although the group was constituted by the previous Congress government, the United Front (UF) coalition government has announced that it will draw on the report's recommendations for future policy. Infrastructure development is not only a declared priority area of the UF government, but also an issue on which there is an impressive consensus across the political spectrum. Infrastructure is also the only area where every political party, including the communists, welcomes foreign investment. Since any change in government this year is likely to feature the return of the Congress Party to power within a coalition (see OADB, January 3, 1997, V), official commitment to all aspects of the report appears assured.

CONCLUSION: The political consensus on infrastructure development should result in the implementation of many of the report's recommendations, even if there is a change in government this year. However, future infrastructure funding depends to a great extent on implementing measures to improve the debt market.

Keywords: AP, India, industry, economy, infrastructure, finance, electricity, telecommunications, debt, energy, investment, foreign investment



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V

IRELAND: Election Economics

EVENT: Finance Minister Ruairi Quinn has presented the 1997 election-year budget.

SIGNIFICANCE: The government's expansionary budget is designed to reverse its opinion poll deficit in the approach to this year's general election. However, a downturn in growth could present serious medium-term problems with regard to public finance.

ANALYSIS: The 1997 budget announced on January 22 is probably the last budget before the present three-party coalition calls a general election. Owing to procedural changes, the 1998 budget will be in November, and the government could technically continue in office until December. However, it is unlikely to delay a poll beyond October.

The 1997 budget provides for:

- a general government deficit of about 2% of GNP;
- an exchequer borrowing requirement of 1.6% of GNP; and
- a projected surplus of current revenue over current spending of about 0.4% of GNP.

This was in the context of a projected increase in government spending of a real 4.5%, which the government accepts as being about 2% too high. The budget also included considerable reductions in direct taxes, increased welfare spending and a cut in corporation tax from 38% to 36%.

Despite the small current surplus, most commentators view the budget as too expansionary, given expected GNP growth of about 5% in 1997. While the government appears to have recognised the dangers of a fiscal policy that tends to be pro-cyclical, the proximity of a general election makes significant adjustments unlikely in the short term.

Economic implications. The budget is pro-cyclical, has failed to hold down the growth of public spending, and could contribute to serious medium-term problems. These could arise as a result of a number of factors:

1. If and when growth slows, built-in stabilisers will produce a serious budget deficit, given existing tax rates and spending programmes.
2. The post-1999 scenario of sharply reduced financial flows from Brussels means that the underlying budget deficit position will become apparent, and will have to be dealt with.
3. Adherence to the Maastricht criteria for Economic and Monetary Union (EMU) and the conditions of the post-EMU stability pact (see OADB, December 16, 1996, I) will limit the ability of governments to engage in anti-cyclical budgetary policy.



Economic growth is likely to continue at or slightly above 5% in 1997. Historically, capacity growth has been considerably lower, at about 3.5%. Optimistic observers believe that there has been a fundamental upwards shift in the capacity growth rate to about 5%. Others are more sceptical, pointing to clear signs of labour market shortages, despite recorded unemployment levels of 11%. While true unemployment is probably much lower, labour market trends do indicate structural and demographic problems. However, these problems are unlikely to be tackled before this year's election.

Industrial peace. The 1997 budget provided a basis for the trade unions to recommend the acceptance of a national, three-year wage and tax pact worked out with the government. The pact, which was formally accepted yesterday, allows for wage increases of 9.25% over 39 months and promises continued direct tax reductions over the period of the agreement. The deal is based on an annual inflation target of just over 2% in the next three years. Although there are rumblings of public sector discontent, the pact holds the prospect of industrial peace without excessive wage inflation.

Political implications. For the last six months, opinion polls have shown the government coalition with support 4% to 8% below the combined support of the main opposition parties. With the opposition's lead sufficient to suggest a change of government, the 1997 budget was designed to provide an election springboard for the ruling coalition. Tax and spending elements were aimed at the target constituencies of the three coalition parties: improved social welfare payments, lower income tax rates on low-to-middle incomes and the abolition of residential property tax paid predominantly by upper-income groups in Dublin. The budget's reception was generally favourable, although as yet no solid opinion poll evidence of its impact has become available.

Political pitfalls. The government's main political difficulties lie in other areas:

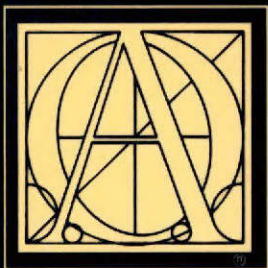
- a minister was forced to resign late last year over dubious financial matters;
- the government has been unable to protect beef export markets, which are threatened by a lack of confidence owing to the bovine spongiform encephalopathy scare;
- scandals carried over from the previous administration, arising from the use of contaminated products in the blood transfusion service, have been badly handled;
- the Irish presidency of the EU, while a diplomatic success, generated little interest domestically -- indeed, the concentration of political attention on the demands of the presidency detracted from the government's ability to respond adequately to domestic problems as they arose; and
- violence is growing in Northern Ireland.

As there is a general consensus about economic policy, the election is likely to be fought on political issues, making it imperative for the government to avoid serious blunders. It also means that the investment climate is unlikely to be affected significantly if the election produces a change of government.

CONCLUSION: If the budget allows the government to regain the initiative domestically, and if it can avoid further political pitfalls, the growing economy, lower taxes and industrial peace provide a solid basis for an election victory this year.

Keywords: WE, Ireland, economy, politics, fiscal, growth, election, government, party, unions





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Specially selected for the World Economic Forum Annual Meeting

Jan 8, 1997: MIDDLE EAST: Economic Reform

SUBJECT: Economic reform prospects for the Middle East in 1997.

SIGNIFICANCE: Egypt's ambition to become a recognised emerging market faces a critical test. The economic progress of Israel's other Arab neighbours is ineluctably linked to the fate of the peace process.

ANALYSIS: The Middle East economic conference, held in Cairo last November, demonstrated vividly the extent to which US/Israeli hopes of integrating Israel within the region have been jolted since the election last May of Prime Minister Benjamin Netanyahu at the head of a hardline Likud-led government. Downgraded by Egypt from the 'summit' status accorded its precursors in Casablanca (1994) and Amman (1995), the Cairo conference was characterised by the host country's emphasis on inter-Arab integration. Although links with Israel were not ruled out, they were made conditional on the Jewish state's honouring of the Oslo accords with the Palestinians and progress towards a broader peace to include Syria and Lebanon.

Even before the Cairo conference, the Palestinians, Jordan and Egypt had begun to signal their displeasure with the Netanyahu government by drawing back from joint projects with Israel and instead directing investment into their own infrastructures. This trend is likely to endure in 1997. At the conference itself, Egypt signed a deal reportedly worth up to 4 billion dollars to supply Turkey with liquefied natural gas -- a deal which would seem to supplant Cairo's previous agreement to pipe gas to Israel, and thence possibly to Turkey. Israel's gas accords with Qatar, signed through the Enron Corporation with much fanfare at the 1995 Amman summit, are on hold. Soon after the Cairo conference, Qatar and Oman froze their respective economic relations with Israel. The opening of Israeli trade offices in the two Gulf states had been one of the key symbols of the economic integration process, a development viewed by Israel as a step towards breaking down the barriers to the Saudi Arabian market.

The renewed primacy of politics in the discourse of the Middle East need not imply a diminution of interest in economic reform. The international gatherings in Casablanca, Amman and Cairo had value in compelling Arab government and business elites to consider their region in the context of the global economy and in terms of competition for capital with other emerging markets. This educative process has been reinforced for those states seeking membership of the WTO or which have concluded, or are still negotiating, association agreements with the EU. There is now in the Arab world an awareness that participation in the world economy requires conformity with the members' rules -- for instance, private sector vigour, capital market development, privatisation, trade liberalisation -- if the dividend of foreign direct investment (FDI) and portfolio flows is to accrue. There is also an awareness that liberalisation does not come without social and political costs.

Governments having weighed these costs and benefits, the pace of reform varies from state to state. There is also differentiation between three increasingly distinct sub- regions:

A. Israel and its neighbours

These are the economies which are ineluctably linked to the fate of the peace process. Developments in regional politics in 1997 -- which could involve a breakdown of Arab-Israeli negotiations, a second Palestinian uprising and/or a fresh flare-up in southern Lebanon -- will therefore have the potential to vitiate investor-friendly economic reform. The economic impact of political events will vary across the sub-region, such are the disparities between the respective economies:

1. Israel. Paradoxically, the US-designated hub of regional integration is the economy best able to withstand a deadlock in the peace process. With the Gulf states having lifted their secondary and tertiary boycotts, Israel has gained its peace dividend -- a boost to its trade and investment links with the dynamic economies of East Asia and an upgrade to its EU relationship. Foreign investment in Israel's high-tech sectors is long-term, and is thus relatively secure in the face of political vicissitudes. Only in the event of a collapse of the peace process, precipitated by an Israeli- Syrian confrontation or an Israeli military reoccupation of the Palestinians' autonomous towns, would Israel jeopardise its investment inflows or access to overseas markets. Such a scenario is possible, but not probable, in 1997.

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Domestic investors manifested a lack of confidence in the stock market in 1996. Their attitude towards equities this year will be conditioned in part by whether Netanyahu delivers on his privatisation promises, and how he chooses to reconcile the contradiction between an austerity budget and the need to reward his coalition allies. The outcome will have an impact on the stock exchange by way of adjustments to monetary policy.

2. **Palestinians.** The outlook for the aid-dependent Palestinian economy is bleak. For as long as Israel fears Palestinian militancy and wishes to block Palestinian aspirations to statehood, it will impose closures to prevent Palestinians from working in Israel, withhold sanction for infrastructure projects (such as the now-completed but still- unlicensed Gaza airport) which are deemed as potentially 'national', and limit Palestinian trade exchanges with Jordan. For its part, the Palestinian National Authority will continue to exert a grip on the territories by preserving an over- bloated public sector. In particular, it will again drain its meagre budget in order to maintain a panoply of security services. The opening of a stock exchange in Nablus early this year will constitute merely a genuflexion to the norms of the global economy.

3. **Jordan.** Hopes of a surge of foreign-investor interest in the wake of the Amman economic summit in October 1995 have long since evaporated. However, pressed by the World Bank, King Hussein and his government are pledged to make renewed efforts towards privatising state monopolies in 1997. As a first step, the electricity and telecommunications companies are to be commercialised. As with previous moves, Jordan will act with caution. Shaken by the spasm of violent unrest last August over the sharp reduction in bread subsidies, the authorities are keenly aware that public opinion needs to be well prepared for economic reforms which entail price rises or job losses.

For as long as the peace process is stymied, the Jordanian government will shy away from new agreements with Israel on regional integration, and most of the private sector will shun joint venture opportunities with Israeli companies. The Jordanian business community still looks to a complete restoration of its once-profitable links with Iraq. However, a lifting this year of the international trade embargo on Jordan's eastern neighbour -- the oil-for-food deal notwithstanding -- is improbable while Iraqi President Saddam Hussein is in power.

4. **Syria.** Nowhere is economic reform more cautious. Talk of unifying exchange rates, renewed in 1996, may not be translated into action even in 1997. Plans for the creation of a stock exchange have long been gathering dust. Preliminary negotiations with the EU on an association agreement have petered out. Syria, which boycotts the multilateral dimension of the Arab-Israeli peace process, spurned the Casablanca, Amman and Cairo conferences. For President Hafez al-Assad, politics is everything. Fearing market economics as a threat to Syria's system of governance, he is most unlikely to embark upon liberalisation in 1997.

5. **Lebanon.** Symbolised by Prime Minister Rafiq-al-Hariri's ambitious plans for the reconstruction of Beirut, the resurrection of commercial Lebanon in the wake of the 1975-90 civil war is the bright spot of the Levant. Eurobond issues over the past two years have been eagerly subscribed by expatriate Lebanese and Gulf investors -- a remarkable statement of faith in the country's prospects by fund holders faced with a myriad of investment alternatives.

1997 will be a critical year for the economic regeneration of Lebanon. The Beirut reconstruction project still requires immense funding if it is to reach even partial fulfilment. An Israeli assault against Hizbollah guerrillas, perhaps involving a deeper penetration than last year's 'Grapes of Wrath' operation (which impelled the flight north of some 400,000 civilians), could deliver a major setback to economic renewal. Moreover, if Syria comes to regard the US-backed 'Friends of Lebanon' campaign, which last month pledged 1 billion dollars in immediate official aid and 2.2 billion in long-term programmes, as a revival of Israel's 'Lebanon first' gambit (aimed at driving a wedge between Beirut and Damascus), it may begin to set limits on its neighbour's economic recovery.

B. The Gulf states

The determinant of reform in this sub-region will be the oil price. Last year demonstrated that the higher the price, the lower the predilection for economic restructuring. Saudi Arabia, with windfall revenues of 12 billion dollars over the year, chose to pay off debts to agricultural producers, state contractors and suppliers.

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It also boosted spending on arms. The kingdom partially obviated the 1995 subsidy cuts and user-fee increases by raising public sector wages. With the oil price expected to settle at around 20 dollars per barrel, or somewhat lower, in 1997, this year's budget (unveiled on December 30, 1996) shows that the Saudi royal family will again take the line that discretion is the better part of valour and, notwithstanding the reformist inclinations of the cabinet's technocrats, pursue an approach broadly similar to that of 1996.

The disincentives to liberalisation and fiscal reform spring from the political and geopolitical circumstances pressing in on the kingdom:

- There is still much uncertainty about the health of King Fahd. While the immediate line of succession is settled, there is a lack of clarity and boldness in decision-making.
- Allegations that Iran instigated the Dhahran bombing last June, coupled with the survival of the present regime in Baghdad, buoyed by the oil-for-food deal, are uncomfortable reminders of perceived external threats. Riyadh's belief that Saudi Shi'ites perpetrated the explosion in Dhahran has reinforced its sense of vulnerability.
- Continuing tension and spasmodic violence across the causeway in the island state of Bahrain serve to strengthen the Saudi rulers' sense that social spending, rather than audacious reform, is an imperative.

The kingdom's Gulf Cooperation Council (GCC) partners are somewhat less inhibited in their approach. Qatar, which pins its hopes for long-term prosperity on massive gas deposits and which is due in the autumn to stage the fourth in the series of Middle East economic conferences, plans to open a formal stock exchange this year. Oman, also investing heavily in gas, is the most committed of the GCC states to fiscal restructuring. In 1997, it will give further serious consideration to the privatisation of the telecommunications and electricity sectors -- a bold advance, if it happens, in the Arab world. The United Arab Emirates is also studying the possibility of opening up utilities; in its case, water and electricity.

However, any tentative moves towards reform will be made in a less than propitious regional economic environment. The six-state GCC, which, since its formation in 1981, could have developed as a model of integration for other sub-regions, is torn by dissension. On account of its territorial dispute with Qatar, Bahrain last month became the first member to boycott one of the organisation's annual summits. Saudi Arabia, hitherto a prevailing force in GCC affairs, failed to persuade Bahrain to reconsider its stand. Oman, traditionally truculent, has signalled its interest in the nascent Indian Ocean rim community, which is due to hold its first summit in March this year. The troubled experience of the GCC, which has yet to realise a cardinal aim of unifying member-state tariffs, hardly bodes well for the Egyptian call for Arab-wide integration.

C. North Africa

From the Atlantic to the Suez Canal, this is the showcase of Arab reformist enterprise. The sole exception is Libya, but even Colonel Mu'ammar al-Qadhafi has recently given freer rein to Tripoli's traders. Elsewhere in the Maghreb and Egypt, privatisation is more advanced than in the Mashreq states and foreign investors are for the most part welcomed. Morocco and Tunisia have signed EU association agreements. Algeria and Egypt hope to conclude their negotiations later this year. Nevertheless, question marks hang over the 1997 liberalisation agendas of all four vanguard reformers:

1. Morocco. Having raised more than 1 billion dollars from privatisations over the past three years, the reform pacemaker now plans a partial sell-off of the state telecoms company. A parliamentary commission began debating last month a draft law which would split telecoms and postal services into two separate enterprises. Foreign investors are to be encouraged to purchase stakes in the telecoms network, including the GSM mobile system.

Privatisation Minister Abderrahman Saaidi has promised that "streamlined procedures" in 1997 will accelerate the privatisation programme, which, in addition to telecoms, is to include the state airline, larger industrial projects and remaining hotels. There is little reason to doubt the government's will, even in the face of domestic criticism of the growing degree of foreign-investor involvement in the economy. The authorities will, however, be wary of sales that would involve significant job losses. High unemployment,

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particularly amongst youths and university graduates, is a troubling feature of the economy, the volatility of which was demonstrated by the severe drought of 1995. Morocco remains prone to social unrest.

2. Egypt. According to the Cairo government, the country attracted last year some 600-700 million dollars in portfolio investment, which contributed strongly to a stock market boom, and pledges of 2 billion dollars in FDI. With the macroeconomy based on sound fundamentals and with the promise of further, regular privatisations in 1997, Egypt has sprung to the attention of foreign investors. Its prospects have been enhanced by earning a place in the International Finance Corporation's index of emerging markets.

There are doubts, however, whether the authorities will honour fully their proclaimed aim of offering to the stock market in the first quarter of this year shares worth 495 million dollars in 15 companies, 13 of which will be majority privatised. Thirty hotels are also to be sold. The doubts emanate mainly from slowdowns in the five-year privatisation drive in 1996. Furthermore, the confidence of foreign investors was shaken last November by the government's surprising decision to withdraw the sale of 51% of the state's holding in Ameriya Cement to Lafarge Coppee of France.

Similar bumps on the road to reform in 1997 notwithstanding, the government's commitment to economic change is firm. Islamist radicals, however, still pose a substantial political risk, and the government must be concerned that much of the foreign portfolio investment is short-term and speculative -- capital which could quickly turn to flight if political conditions were to deteriorate.

3. Tunisia. Once perceived as a pacesetter, Tunisia has often promised rather more than it has delivered. Pressed to do so by the World Bank, it is about to embark on a renewed privatisation push. Tunisia plans over the next five years to extend state sell-offs to strategic sectors, including the state banking system. This year, in the opening phase, it aims to privatise 63 public firms, including cement companies and stakes in national carrier Tunis Air and the oil distribution company, Societe Nationale de Distribution de Petrole. If the government is to abide by its schedule, further promptings by the World Bank may well be required.

4. Algeria. With market economy and investment guarantees embodied in the new constitution, efforts to transform the state-run, oil-dependent economy into one that is more diversified and private sector-oriented are about to gain a fresh impetus. Further privatisations are planned for 1997, and a bourse is to be established within three to six months. However, the pace and depth of restructuring will be circumscribed by the civil conflict. In particular, the authorities will be loath to augment significantly the huge number of unemployed in Algeria's cities and so strengthen the recruiting potential of militant Islamist groups. Moreover, the military will seek to preserve its vested interests. With political killings still part of daily life, only the relatively violence-free hydrocarbons sector is likely to attract foreign investors in 1997.

Dual containment states. Ironically, given the marketising efforts of their rivals in all three sub-regions of the Middle East, Iraq and Iran -- the former still the subject of a UN trade embargo, the latter the target of US sanctions -- are highly desirable foreign investment destinations. Both have major oil industries and other sectors which are in need of post-war reconstruction. Both, however, may remain off limits in 1997: Iraq, because the oil-for-food deal will not lead to a further easing of sanctions until Saddam is overthrown; Iran, because major investors will be deterred by the extraterritorial provisions of US legislation.

Favouring a change in US policy towards Iran, business lobby pressures on the Clinton administration will mount in Washington in the hope that the president will relent as he did in the case of Vietnam. However, even if Washington were to offer an olive branch to Tehran in the aftermath of the Iranian presidential election, due next May or June, there can be no guarantee that the new Iranian leader would respond positively. He may turn out to be less pragmatic than the present incumbent, President Ali Akbar Hashemi Rafsanjani. He would also still need to contend with spiritual leader Ali Khamenei and other anti-US conservatives. However, if allegations of Tehran's involvement in the Dhahran bombing are substantiated, the prospect of a US initiative aimed at a rapprochement with Iran will rapidly recede.

World economic environment. In seeking to become established as emerging markets, reforming economies in the Middle East join a fierce competition for international capital. For many years, East Asia and Latin America have captured most of the foreign investment destined for the developing world. The East European experience has demonstrated how difficult it is to break the mould. Thus, even bold liberalisation by Arab states will be no guarantee of funds so plentiful as to transform their economies. Moreover, with

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interest rates set to rise in the industrialised world, emerging markets -- especially new ones such as Egypt and Morocco -- could lose their allure in 1997.

The crucial challenge for all Arab states this year is whether, like Lebanon, they can begin to attract back expatriated capital, which is estimated to amount to as much as 800 billion dollars. When Arab residents and Arabs overseas invest in their own countries, Arab economies will have passed the reformist test.

CONCLUSION: Even in North Africa, where the reform process is at its most adventurous, restructuring will be constrained by political and social considerations. In the context of global investment opportunities, Middle Eastern emerging markets will remain marginal.



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*Printed for the World Economic Forum Annual Meeting
Davos 1997*

Oct 28, 1996: UKRAINE: FDI Outlook (E)

SUBJECT: Foreign investment in Ukraine.

SIGNIFICANCE: Attracting foreign capital will be crucial if the sharp decline in capital investment of recent years is to be reversed and the economy revived.

ANALYSIS: Ukraine possesses substantial natural resources (particularly mineral), a comparatively well educated workforce and low labour costs. Geographically, it is well located with respect to both Russian and Central and West European markets. However, the republic has largely failed to attract the attentions of foreign investors:

- Foreign direct investment (FDI) from all sources in 1991-95 amounted to only 750 million dollars, compared to an end-1995 stock of 10.7 billion for Hungary, for example (see EEDB, May 16, 1996, II).
- FDI from outside the CIS in 1990-95 has been estimated at only 574 million dollars. Moreover, some western estimates suggest that Ukraine's share of outside investment into the former communist bloc will decline between now and 2000.
- At the end of the first quarter of 1996, Ukraine's FDI stock amounted to 17.6 dollars per person, one of the lowest per capita figures in Eastern Europe.

Serious obstacles to foreign investment inflows remain:

1. Poor market reforms. Economic reform since independence has been relatively slow and market mechanisms and institutions are under-developed. Administrative interference in economic affairs is common, particularly on the part of local officials; economic legislation changes frequently; legislation establishing a market framework for many aspects of economic activity has yet to be adopted; privatisation has been slow (see EEDB, June 6, 1996, I); there are restrictions on private land ownership; the tax system is confiscatory; and there is considerable uncertainty about the future of economic reform.

2. Crime and corruption. Economic life is highly criminalised, and corruption is widespread. Outsiders face particular difficulties in attempting to operate in an environment where the second economy -- with its reliance on networks of contacts and local knowledge -- accounts for perhaps 40% of economic activity (see EEDB, October 21, 1996, II).

Improvement signs. However, the acceleration of economic reforms since 1994 has affected FDI inflows. Last year saw the largest annual inflow to date -- 266 million dollars -- and inflows in the first quarter of 1996 amounted to 137 million dollars, bringing the total to 887 million. Coca-Cola has invested over 100 million dollars and plans to invest another 250 million over the next two years, while Shell, Procter & Gamble and other major western firms have also begun to invest in Ukraine.

The largest investment share comes from the United States (23%), followed by Germany (18%), the United Kingdom (6%), Cyprus (5.1% -- a reflection of its position as a favoured destination for flight capital from the former Soviet Union) and Russia (5%). However, Russia's share is underestimated, because much Russian investment takes place through channels not reflected in official statistics.

Among the factors which have contributed to larger FDI inflows are:

- the adoption this year of a new constitution (see EEDB, July 3, 1996, I);
- work on the adoption of a civil code modelled on the German example;
- the passage of key economic legislation, particularly a law 'On the Regime for Foreign Investment';

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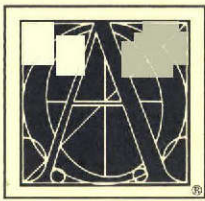
- progress towards financial stabilisation (see EEDB, September 6, 1996, II); and
- the adoption of tough measures to reduce economic crime in the state sector.

Foreign investment law. The law on foreign investment is designed to create a favourable climate for foreign capital. It includes a section on state guarantees for the protection of foreign investment, and provides for national treatment for outside investors -- although the value of this might be questioned, given the generally difficult climate in which Ukrainian entrepreneurs currently operate. The law does not provide for tax holidays and other privileges for foreign investors, but it does allow for the extension of tax breaks and other privileges via legislation in the cases of investment projects seen to be of particular importance. The law also stipulates that foreign investments are not subject to nationalisation and that investors have the right to compensation for any losses suffered as a result of improper actions on the part of state institutions or individual officials. Repatriation of profits, income and other funds legally received is guaranteed (after payment of taxes and other mandatory payments to state funds).

State registration of foreign investments is to be carried out by executive organs within three working days --- considerably quicker than in Russia. The authorities are no longer allowed to refuse registration on such grounds as 'inexpedience' or 'undesirability': a refusal must be based on some specific provision in law. In theory, at least, registration has therefore effectively become a process of informing the authorities of an investment rather than seeking their permission. The law also stipulates that some areas of the country could be closed to foreign investors on security grounds; no region is mentioned by name, but this could well refer to places such as the Zheltogorsk area, which have uranium deposits.

On balance, the law represents progress towards the elimination of barriers to foreign investment. However, Ukraine will become a more attractive destination relative to neighbouring countries only if progress is also recorded in fields not linked specifically to foreign investment -- the question of private land ownership in particular, remains unresolved, while market conditions as a whole need to improve. However, even if this is achieved, Ukraine seems unlikely to benefit from massive inflows of western capital. A substantial increase in Russian investment is somewhat more likely, particularly if sources of friction between the two countries are eliminated and trade barriers reduced.

CONCLUSION: Foreign investment inflows into Ukraine will probably continue to pick up. However, the increase will be modest and there is unlikely to be any sharp rise in FDI in the medium term.



16282

20th February 1997

Jim Wolfensohn
Country Department III
World Bank
1818 Street NW
Washington DC 20433

President Has Seen

Dear Jim,

In an effort to have something that you can reach to for quick reference on what's happening or likely to happen around the world this year, we have decided to bind the Daily Brief coverage which was undertaken between December 31st and 8th January. These are the pieces, you'll recall, that looked at the year ahead.

We trust you'll find them useful. Do let us know if you wish additional copies for any colleagues.

Yours sincerely,

David R. Young
Managing Director

*P.S. Was good to see you in Dorset.
Must discuss your next letter at
some point.*

**Oxford
Analytica
Ltd.**

5 Alfred Street
Oxford OX1 4EH, England
Registered office at the above address.

Telephone:
Oxford (44-1865) 261600

Fax:
(44-1865) 242018 or
(44-1865) 261626

E-Mail: oa@oxford-analytica.com
Telecom Gold Mailbox No.87:WQQ666

Registered in England: No. 1196703
VAT No. GB 533 1281 76

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