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McNamara Papers

~~Mr. McNamara's Chronological file~~ (Incoming)
~~from March - December~~ 1971 (Jan-June)

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President's papers - Robert S. McNamara Chronological files (incoming) - Chrons 06

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May 21, 1971

Mr. Takeshi Watanabe
President
Asian Development Bank
Commercial Centre
P.O. Box 126
Makati, Rizal D-708
Philippines

Dear Mr. Watanabe,

In the absence of Mr. McNamara, I am pleased to enclose for your information a copy of a secret note on recent discussions with the Government of Pakistan and a possible course of action for the Consortium. This is the note referred to in Mr. McNamara's message to you of May 14, 1971.

Sincerely yours,

I. P. M. Cargill
Director
South Asia Department

Enc.

cc. Mr. L. Christoffersen

President has seen

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5-21-71

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

H 4200

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PAKISTAN

A Note by Mr. Cargill on Recent Discussions with the Government and a Possible Course of Action for the Consortium

Discussions in Pakistan

1. As you know, I visited Islamabad from May 1 - 4. My visit had two principal purposes: (i) to ensure, to the extent possible, that the central authorities, in particular President Yahya Khan, understood how severely Pakistan's image abroad had been damaged by reports on the actions of the army in East Pakistan and how this might act as a constraint upon aid from abroad, and (ii) to examine further Pakistan's financial situation and short-term outlook.

2. The information provided by authorities on Pakistan's finances leaves no room for doubt that the situation is extremely serious. The foreign exchange position and outlook for the period May through September are described in detail in Annex I. In brief, all available evidence suggests that sometime in July or early August Pakistan will probably have exhausted the State Bank's exchange assets in convertible currency. This is after taking into account the Government's announced intention to defer roughly US$55 million of debt service payments in foreign exchange during the period.

3. The internal financial situation is equally serious. The Government now expects to have to obtain Rs 1,650 million (US$350 million) from the banking system to finance the budget deficit in 1970/71. This compares with an original estimate of Rs 600 million for the current financial year. Expansionary financing at such a level would exceed by 25 percent the previous peak reached during the war with India in 1965/66. It would be needed to support a level of public development expenditures in real terms substantially less than last year and roughly equivalent to that achieved four or five years ago. Indeed, considering that expansionary financing of the budget had already reached Rs 1,350 million by the end of February - that is, before all revenue collection stopped in East Pakistan - the Government's present estimate of the budgetary financing gap may well prove too low.

4. In sum, it is evident that the suspension of economic activity in East Pakistan, superimposed as it was on a deteriorating trend resulting from the Government's procrastination in undertaking the comprehensive exchange and revenue reforms that have been under discussion for some time, has led to crisis conditions in both the external and internal financial situation. Furthermore, the repercussions of this situation are bound in a few months' time to spread to West Pakistan, unless (i) the economy in East Pakistan is restored quickly, both as a market for West Pakistan's manufactures and as an earner of foreign exchange, and (ii) very substantial amounts of external

assistance are committed soon. If normality - in respect of economic activity in East Pakistan and in respect of external assistance - is not restored quickly, it is difficult to see how West Pakistan can avoid a sharp reduction in industrial activity, with the possible consequence of widespread social unrest.

5. Annex II examines the amounts of external assistance that might be needed for 1971/72 to avoid complete exhaustion of the State Bank's exchange assets in convertible currency and to prevent imports from falling to a level at which a severe cut-back in economic activity will become unavoidable. More work has to be done to firm up these estimates. However, as a very rough indication of orders of magnitude, it appears that, excluding project aid, at least US$500 million might be needed for these purposes, including perhaps US$175 million in a form equivalent to cash (i.e. IMF resources and debt relief), US$200 million for imports of foodgrain, and the rest in commodity aid. Furthermore, a substantial part of this assistance, particularly the cash portion, would have to be committed no later than the end of July; arrangements for food aid may have to be made even earlier. Shortfalls in export earnings below the optimistic assumptions underlying these calculations would require additional commodity aid, to replenish the pipeline, around the end of the calendar year.

6. As noted above, these very rough first estimates are subject to change as further work is being done, but the basic facts as outlined here will remain: if Pakistan's economic collapse is to be prevented, action will have to be taken quickly and the amounts of external assistance required will be large.

7. Against this economic background and on the presumption that progress towards economic stability in Pakistan and the willingness of the outside world to help are contingent on resolution of the political crisis, I found the discussions of the political situation - with President Yahya Khan and senior officials - highly disconcerting. They left me with the strong impression that the greatest difficulty confronting any effort by the Consortium countries and the Bank and the Fund to help Pakistan achieve a viable solution to the present crisis is the inability of those in authority there to see the facts as they are.

8. Yahya Khan spent a great deal of time explaining why he felt compelled on March 25 to instruct the West Pakistan troops to restore law and order in East Pakistan. However, whatever the truth of the events leading up to this decision, the essential purpose of my discussions was to find out how the Government proposed to resolve the present crisis. It was at this point that I came to feel that all dialogue between the Government and the outside world was likely to be fruitless, simply because it appeared that the two sides would be talking about two different sets of facts.

9. When I was in Islamabad, censorship in Pakistan was still complete and there was strong evidence that unpleasant news was being withheld from the President. Even the most senior officials believed that what happened in East Pakistan was a minor police action aimed at removing from the political scene

a limited number of secessionists, that this was over and that the disruptions caused to economic and social life would soon be ended. President Yahya Khan was obviously unaware of the reactions in the outside world to reports of the army's actions in East Pakistan and, until briefed immediately before the discussions, did not know how desperate the country's financial position was. Furthermore, he stated unequivocally that the army had essentially completed the first phase of its operations, the restoration of law and order, and that normality was fast returning to East Pakistan.

10. As to the future, Yahya Khan spoke with apparent sincerity of his intention to hand over the administration to elected civilian authorities. He envisaged early establishment of a provincial government in East Pakistan, on the basis of an interim constitution which was being drawn up to reflect the agreements reached with the Awami League by March 25. To this end, he proposed to invite the representatives elected last December to form a provincial legislature. Elected members of the Awami League would be free to establish, under another name, any party they wished. Preparatory discussions were already under way with East Pakistan politicians.

11. Finally, as regards the economic situation, President Yahya Khan indicated his readiness to accept any reform program the Fund and the Bank considered necessary to overcome the financial difficulties and secure assistance from abroad. He declared himself satisfied that stocks of foodgrain in East Pakistan were adequate for the time being and that every possible precaution was being taken against the outbreak of widespread famine. The President went on to say that once the needs of East Pakistan were determined, relief supplies from abroad would be welcome, but their distribution would have to be left to Pakistani agencies, because he was not going to let the army do the shooting and then have foreigners handle the distribution of food.

12. As I said before, my greatest difficulty with this exposition of the situation and plans for settlement was that it appeared to be unrelated to the facts as they had been reported by other sources. Thus, it is difficult to reconcile the President's approach to a political solution with the army's actions in East Pakistan which, by all accounts, went far beyond restoring law and order. Furthermore, even while the President spoke of peace having been restored in East Pakistan, diplomatic reports reaching Islamabad said that destruction of property and the harassment and killing of people continued unabated. In any event, the only East Pakistan politician of any stature with whom the President seemed to have spoken at the time was Nurul Amin, a Muslim leaguer, with little, if any, political following; and even he declined to take the lead in trying to form a government in East Pakistan.

13. In short, the realism of Yahya Khan's plans for a political settlement is open to serious questions. It seems by no means clear that the army would be prepared to accept a settlement along the lines proposed. Also, it is extremely doubtful that a government of the kind envisaged could be formed in East Pakistan,

after all that happened after March 25, or that its leaders would long survive its formation. Finally, unless economic conditions in East Pakistan return to normal quickly, it is difficult to see that an economic program appropriate to the circumstances could be drawn up which the Government would be prepared to accept and able to put into effect in all of Pakistan.

Discussions in the United States

14. Mr. M.M. Ahmad, Economic Adviser to President Yahya Khan, accompanied by Mr. Sartaj Aziz, Joint Secretary, Planning Division, was in Washington from May 10 to 16. He met with President Nixon, Secretary Rogers and Mr. Kissinger as well as Dr. Hannah and Mr. MacDonald at AID and Mr. Sisco at the State Department. He also had discussions with Mr. Schweitzer at the IMF and Mr. McNamara at the Bank, as well as with the staff of the two organizations. Before proceeding to London, Mr. M.M. Ahmad also met with the Secretary General of the United Nations on May 17 to discuss the possibility of the UN organizing an international relief effort to prevent widespread famine in East Pakistan.

15. In their meetings in Washington the delegation dealt at length with the Government's account of the origins of armed intervention in East Pakistan, and essentially repeated what has been said above about the Government's view on the situation in East Pakistan and the President's plans for reaching a political settlement. On the financial and economic situation, they made the following points:

(i) Pakistan faced a very serious liquidity crisis and exchange assets were likely to be exhausted by August. Financial assistance, in appropriate form, was needed quickly if the crisis was to be averted. They were looking to the IMF for such assistance, in the context of an exchange reform.

(ii) The Government of Pakistan was aware that the suspension of debt service payments to Consortium countries was complicating their relations with the Consortium. They were therefore anxious to resume full payments, but lacked the resources to do so, save by means of an emergency drawing on the IMF.

(iii) A sharp deterioration in the economy of West Pakistan later in the year would become inevitable unless aid relations with the Consortium were normalized quickly, new commitments, essentially of commodity aid, made promptly to replenish the pipeline, and early agreement reached on debt relief on a longer term basis.

16. As I see it from the accounts given to me by Mr. M.M. Ahmad of his meetings outside the Bank, a common theme ran through the responses given to the presentations by the Pakistan delegation. Most generally this was that, understanding for the tremendous difficulties of resolving Pakistan's problems and willingness to help notwithstanding, there was at the present time no basis

on which financial assistance could be given. Pakistan's present image in the world and its effect on public opinion had created for the Governments of aid giving countries very strong constraints, and there was no economic program to serve as the framework for external assistance. It was up to the Government of Pakistan to remove these constraints by demonstrating, in terms of concrete action, that it was capable, by following the approach indicated, of achieving a political settlement, that held out the promise of restoring political stability, and of undertaking the necessary economic reforms.

17. Another issue that came up in the discussions was the food situation in East Pakistan. Grave concern was expressed about the prospect of widespread famine there which, if allowed to occur, would destroy all prospects of normalizing Pakistan's relations with the Consortium. I understand that the US Government made it clear that they stood ready to resume shipments of food to East Pakistan, provided the Government of Pakistan made appropriate arrangements, and to join in an international relief effort under UN auspices.

18. More specifically, the US Government turned down as inopportune the delegation's request for early conclusion of a commodity loan under this year's pledge, preparation of which had been held in abeyance, and advised the delegation that, before any decision was taken, they would wish to have the findings and conclusions of the Fund and the IBRD. Mr. Schweitzer explained that he could not see a basis for an emergency drawing and that any use of the Fund's resources would have to be in the context of an economic program, preparation of which would require a mission to visit Pakistan to review the situation and consider, with the Government, the appropriate elements of a reform program. Mr. McNamara said that in his view the Bank could most effectively help Pakistan in the present difficult circumstances by assisting the Government, in close collaboration with the IMF, in drawing up an economic program that could serve as the framework for consideration by the Consortium of Pakistan's needs for external assistance. However, he emphasized that, as he saw the situation, political considerations were the dominant constraint on external support for the time being. Only the Government, by its actions, could overcome this constraint, and he urged the delegation during its stay abroad to try to understand its strength. Mr. McNamara added that the reply sent by Yahya Khan to the United Nations on its offer of assistance in organizing an international relief effort was widely interpreted as telling the UN to keep out of the situation and therefore had tended to worsen rather than improve the general climate.

19. It should be noted that by the time Mr. M.M. Ahmad saw the Secretary General of the United Nations on May 17 the Government's attitude towards UN involvement had apparently changed considerably. At that meeting, he invited the United Nations promptly to send staff to Dacca to help assess the Province's requirements and initiate discussions on administrative arrangements.

A Possible Course of Action

20. Thus, the situation we are facing is this: The Government says that conditions in East Pakistan are fast returning to normal and that it is working towards a political solution which it expects to restore political stability and thereby establish a framework, politically as well as economically, for normalizing

its relations with the Consortium. The general consensus in the Consortium seems to be that the Government's view of the situation in East Pakistan conflicts with the facts and that its plans for bringing about a political settlement are unrealistic.

21. However, the only feasible course, short of inaction, is to give the Government the chance of demonstrating that its approach is workable. Thus, to make possible the provision of adequate external aid it would be essential that (i) conditions conducive to restoring normal life would be created in East Pakistan; that the prospect of widespread famine in East Pakistan be averted by appropriate arrangements with the United Nations, probably involving UN observers stationed in East Pakistan; that sufficient progress be made towards a political settlement to demonstrate the effectiveness of the Government's approach; (ii) that on the economic front the Government, in consultation with the IMF and the Bank, work out a reform program - involving in particular the exchange and revenue systems, with the assurance of equitable treatment for East Pakistan being one of the prime objectives of these reforms - to serve as the basis for consideration by the Consortium of external assistance.

22. On this basis, it was agreed between the Pakistan delegation and the IMF and the Bank that

(a) a Fund mission, accompanied by Bank staff, would visit Islamabad as soon as practicable for a comprehensive review of the economic situation and discussions of an appropriate package of measures for the reform of the exchange system;

(b) The Fund's mission would be preceded by a Bank mission, accompanied by Fund staff, to East Pakistan to assess the outlook for normalization of the economic situation and functioning of the provincial and local administration as well as the related balance of payments and fiscal outlook. Their findings are intended to assist the Fund mission in determining what an appropriate reform package would comprise and in judging the prospects for effective implementation of a package.

23. The Fund mission will be led by Mr. Gunter, the Bank mission by myself. The Government of Pakistan has now confirmed that the mission to East Pakistan can start its work about June 1 and the Fund begin its discussions in Islamabad around June 10. Both missions are expected to complete their work by June 18 or 19.

24. Meanwhile, it is hoped that substantial progress will be made by the Government of Pakistan in reaching agreement with the United Nations on the volume and kind of relief supplies needed for East Pakistan and on administrative arrangements to give donors the assurance that their contributions will serve their intended humanitarian purposes.

25. On the assumption that the time table outlined in paragraph 23 will prove feasible, there will be a meeting of the heads of delegations in Paris on June 21 and 22 as the Bank and Fund missions return from Pakistan. This would be the Monday and Tuesday following the meeting of the India Consortium on June 17 and 18. The purpose of the meeting will be to inform the members of the Consortium about the findings and conclusions of the Bank and Fund missions and to consider what the next steps should be. If appropriate, the possibility of replacing the present so-called moratorium by other arrangements for debt relief - which would be more equitable, include arms credits, and extend through the end of 1971 - may also be discussed. For the moment, plans for the meeting on Pakistan must obviously remain subject to confirmation as the situation becomes clearer.

South Asia Department — I.P.M. Cargill
May 21, 1971

~~June 18~~

489/3/9

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT
ASSOCIATION

INTERNATIONAL FINANCE
CORPORATION

OFFICE OF THE PRESIDENT

6/9 TO Mr. Votaw

1) Greg - Please draft a suggested reply

2) Was there a "majority" cable - if so send me a copy

RSMcN

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6/18

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JUN 9 REC'D

EMBASSY OF PAKISTAN
2315 MASSACHUSETTS AVENUE, N. W.
WASHINGTON, D. C. 20008

June 7, 1971

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WBG
ARCHIVES

AMBASSADOR OF PAKISTAN

Dear Mr McNamara,

You may be interested in seeing the enclosed transcript obtained from the WETA, the local television station as it makes a reference to you and the World Bank.

Warren Una was formerly on the staff of Washington Post and has been often posted abroad to represent the Washington press. Though he is a fairly well-known political correspondent and commentator on South Asian affairs, I have no doubt that he has indulged in gross exaggeration during his television appearance on May 28. I am sure no official in the World Bank, no matter how emotional, could have given him any such information, (as regards that "nasty cable" or the alleged decision of the Bank that "they are not going to get anything").

With my best regards.

Yours sincerely,

(A. Hilaly)

The Honourable
Robert S. McNamara
1818 H. Street, N. W.
Washington D. C. 20433.

FOR EMBASSY OF PAKISTAN

PROGRAM NEWSROOM STATION WETA TV

DATE May 28, 1971 6:30 PM CITY Washington, DC

U. S. TAKES HARD LINE WITH PAKISTAN

NEWSCASTER: There's some evidence that the United States has decided to take a hard line with Pakistan despite some reports to the contrary.

And Warren Una has that story.

WARREN UNA: Well, the United States has been mollycoddling Pakistan since the mid '50's but it's finally decided to get tough. President Nixon told President Yahya Khan of Pakistan in no uncertain terms recently that the U. S. is not going to bail them out of their latest need which arose in the March 25th suppression of the Bengali movement in Pakistan's eastern half, East Bengal. And it resulted in a fratricidal war and terrible destruction of -- certainly of -- human lives but also the whole economy there.

Up to now Pakistan's been getting about two hundred million dollars a year in economic aid and something like ten million dollars a year in credit sale -- military credit sales.

Now, despite the President's decision President Yahya Khan told a press conference in Karachi earlier this week that he had what he said was a very warm, kind personal letter in which Mr. Nixon offered to do anything he could to help.

Well, this is an old trick in Pakistan. They've been hogswaggling us for quite a while. Secretary Dulles was under President Eisenhower. The Pakistanis went to him and said the Turks are very anxious to get into an anti-communist pact, if only you will join. And then they ran to the Turks and said, the Americans are very anxious to get into an anti-communist pact, if only you Turks will come along.

And while Dulles was still thinking about it they started putting in the press that military arms were coming. So, this is no new technique.

Now, what happened is that Pakistan is now broke. And its earnings are in a mess. And there has been known demonstrable interest in caring for the 78 million Bengalis. In fact something like three and a half million of them have had to flee into India and become a burden on that already over-populated country.

And also the majority of the Bengalis have been sort of disenfranchised now even though their party won the majority in the recent election. Few foreigners have been permitted in to see any of this. The press was kicked out when it first happened.

But Pakistan's chief economic advisor, a man named MUZAFFER ~~Lazaher~~ Ahmed (?) was sent here a few weeks ago to try and make people understand the need for his country. And two Pakistan newsmen came and sort of -- half government, half newsmen -- to try and sweeten the press.

Now Robert McNamara, the head of the World Bank which has taken a very hard stand on this because it's a business organization and they see a risk when they -- after studies --, went to both Henry Kissinger and the President before Ahmed came. And sort of stiffened the President's stand on this despite the Pentagon's usual plea that Pakistan is a good military ally and we must keep going.

This caused the President to lay down the line to Ahmed when he came. Also to Agha Shahi, their ambassador to the U.N. and this letter to President Yahya. And said it in a way -- and I've talked to people who've seen the correspondence -- that he appreciates -- Pakistan's a good friend -- but the Congress and the people of this country will never understand that the United States takes its now scarce resources to give money to Pakistan under this circumstance unless it does something to politically reconcile its other half, not just with military needs. So, all that's going through is really food and medical relief.

And today the World Bank and the International Monetary Fund sent a team out there going by way of Japan which also is a big aid to Pakistan group. However, the World Bank has already learned that the people that they mean to interview in Dakka, the reliable government and hard working civil servants, have been ordered out of Dakka when the Bank team and the IMF get there to Islamaba (?). And when the Bank and IMF team get to Islamabad these people are supposed to be quickly sent back to Dakka.

So, the Bank sent a nasty cable the other day saying, look, you're not going to fool us. We're going to look and we're going to find. And then they're coming to Europe for a consortium of the aid to Pakistan friends on June 21st to see what aid should be given. Pakistan wants something like I think up to a hundred and twenty-five million loan by June 30th and then another three-hundred million through the next fiscal year. I gather that the Bank's decision is just about made. They're not going to get anything. They just feel that there's an impossible situation.

The State Department was a little behind this time in getting the word. And the other day their spokesman referred to it as an internal affair and said that the United States has cautioned both governments to restrain themselves, putting India -- equating India -- as equally to blame as Pakistan.

Pakistan, by the way, has already started repeating the line, if you and the United States don't give us we'll have to go to China and she will.

NEWSCASTER: Is that likely to change our mind on this decision, Warren?

UNA: I don't think so.

Now, this is just too -- let's say outrageous. It's an editorial expression but I think when a country decides to shoot down so many of its own population and then not to seem to care about its rehabilitation others just can't look the other way.

FORM NO. 57 INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: June 2, 1971

FROM: Munir P. Benjenk MPB

SUBJECT: Regional Work of the Bank on the Middle East

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1. In July 1967 a special task force was set up within the Bank to study possible projects in the Middle East that might have a significant development impact and promote prospects for political stability in the area. Special attention was to be given to the problem of employing the large numbers of Arab refugees. Major sectors identified for study were agriculture, industry and tourism. In addition, the need for manpower training was to be reviewed.

2. The task force was active for about one year. Copies of a briefing prepared for yourself on April 29, 1968 and of a position report dated August 13, 1968 are attached. They show that although considerable development potential exists in the region it was difficult to identify projects which would have a significant impact on the employment situation and at the same time be politically palatable to the countries concerned. In agriculture, for example, the land and water resources in the Jordan Valley are limited and could not provide a basis for large-scale settlement of refugees. The countries in the Tigris-Euphrates Basin and the Sudan, on the other hand, which offer much greater possibilities for agricultural development, were considered unlikely to accept a sizable immigration of Palestinians. Moreoever, it became evident that a large and increasing number of refugees no longer has an agricultural background and would be reluctant to accept rural employment. Prospects for tourism development are good in the area but their realization depends on a peace settlement. Industrialization and services probably hold the key to a solution of the employment problem.

3. After mid-1968 the subject was not further actively pursued within the Bank. However, contacts were maintained with the Rand Corporation which had done similar research. A list of studies issued or under preparation is attached. Some of these studies, especially the ones dealing with political problems, are well done. The draft volume on oil (July 1969) is partly outdated and generally underestimates the growth of demand. A study on the agricultural potential of the Middle East has just appeared; an earlier draft was reviewed by the Projects Department and received low marks. The study on economic development in the Middle East is not yet completed; but individual country papers on which it will be based have been issued and are of mixed quality.

4. More recently, prospects for economic development in the Middle East have considerably improved in the light of the large additional resources that have become available to the region after the increase of

oil prices (Teheran and Tripoli agreements). For 1971 alone the oil receipts of Middle-Eastern countries (excluding Iran but including Libya) are estimated to rise by about \$3 billion, from about \$4.6 billion in 1970. Further increases are expected for the following years. Unfortunately, very little of these funds will go directly to countries immediately affected by the refugee problem (i.e. Jordan, Lebanon and Egypt). But through the Kuwait Fund and bilateral transfers they might be able to capture a somewhat larger share of the additional resources. In the next few years, the oil revenues of the UAR, while still small when compared with the Gulf States and Libya, will make an increasingly important contribution to Egypt's resources.

5. I would conclude that another study is not what is needed now, but rather a drawing together of all available studies into an action-oriented strategy for the first five years after a peace settlement.

v. But preparation of [illegible] 5 yr post-war country progs for: Jordan, Syria, Iraq, Lebanon, UAR with some indic. of possible financing might be helpful

Attachments

What is the objective
1. reg. integration as stimulus to peace or as glue to preserve a peace
or v. a brighter nat'l devel. prog. as a carrot to move to peace

1. Regional devel. plans do not appear practical
3. Try to develop plans for absorption of refugees
4. Plan for reopening of Suez Canal

I.U. Bank Objective: Development of Mid-East in a modern terms once peace has been restored in area"

Approach:
1. a ltr from Sec Gen to W Bk stating help toward 1 or 2
v. Need to obtain major donor & Bd approval to approach countries concerned
3. with approval of all parties, Bk to:
a. assist in preparing 5 yr accel devel prog
b. "organize" a consortium to finance

Attachment

NOTE

SUEZ CANAL AND FUTURE EXPANSION

I. Physical Aspects

Existing Canal Facilities

1. With the Bank loan given in December 1959 to the Suez Canal Authority (SCA), the Suez Canal was deepened to an average depth of 50 feet (it varied from 48-52 feet depending on the section of the Canal involved) and widened to achieve a cross sectional area of 1,800 square meters necessary for a minimum acceptable ratio of 1:5 between the wet cross section of the ships and that of the Canal. As a result, ships with a draught of 37 feet and a deadweight tonnage (dwt) of 46,000-50,000 tons could go through the Canal.

2. In 1964, SCA obtained a $27.4 million loan from the Kuwait Fund to deepen the Canal further, to permit ships with draughts up to 39 feet to go through the Canal by June 1967, and those with up to 40 feet draught, by early '68. The cross section of the Canal was to remain at 1,800 square meters. This deepening would have permitted passage of ships of between 65,000-70,000 dwt. However when the hostilities broke out in mid-1967, the work planned up to June 1967 had been more or less completed.

3. In the circumstances, the Suez Canal today has an 1,800 square meters cross-sectional area and depth that could accommodate ships with draughts around 38-39 feet and a dwt of between 60,000-65,000.

Expansion Planned At The Time of Mid-1967 Hostilities

4. SCA had engineered a further expansion program, to be implemented immediately on completion of the Kuwait Fund financed work and to be completed by 1972. This program had not only been fully engineered, but tenders for the works involved had been received and evaluated when the hostilities were resumed in mid-1967. The program involved the deepening of the Canal to an average of 58 feet to accommodate ships with draughts up to 48 feet and a dwt of 110,000-125,000. This depth would have required a widening of the cross-sectional area of the Canal to 2,400 square meters. However, since SCA was planning to deepen the Canal further after 1972, it intended to straight away widen the Canal for a cross-sectional area of about 3,100 square meters as part of the expansion program. The purpose of completing all the widening at one time was to avoid the additional cost of building temporary revetments (which lie on the Eastern Bank of the Canal) for a 2,400-square meter cross section, which would then have to be displaced in order to have the wider cross section for a deeper Canal after 1972. The Expansion program, including dredging, maintenance, navigational and signalling equipment, was estimated to cost about US $211 million.

Current Plans for Expansion of Canal

5. As in the past, oil tanker traffic should continue to be the staple source of revenue for the Suez Canal. Since the above-mentioned expansion program could not be implemented, SCA in the meantime has formulated a more ambitious program for the expansion of the Canal taking into account the latest trends towards very large oil tankers. This program could be executed in three successive steps:

(a) Step 1: The Canal will first have to be cleared for navigation by removing wrecks,submerged mines, etc., and slightly dredged, mainly to remove some silting, to permit passage of ships with draughts up to 39 feet. SCA expects this work to be done within 4 to 6 months. Further 4 to 6 months work will be needed to increase the Canal's depth for ships with draughts up to 40 feet. With these works, the 1964 project financed by the Kuwait Fund would in essence be completed. Together with some new navigational, maintenance and workshop equipment to replace those badly damaged by the 1967 hostilities, Step 1 could involve an expenditure of between $15-20 million.

(b) Step 2 essentially seems to be a slight modification of the 1967 expansion proposal (para 4 above). It involves deepening of the Canal to an average of 62 feet and widening the cross-sectional area to about 3,100 square meters, to permit passage of ships with draughts up to 53 feet and dwt up to 150,000 tons. To obviate expenditure on placing temporary revetments, since the Canal is to be deepened and widened further, SCA plans to cut and place 150 kms of permanent revetments at a point necessary for a cross-sectional area of 4,200 square meters. This step could take between 2 to 3 years to complete, and involve dredging of a volume of about 300 million cu. meters. The detailed engineering for this step is apparently complete.

(c) Step 3, visualizes the deepening to an average of about 75 feet, in order to accommodate ships with a draught of 67 feet and dwt of 260,000 tons (or 290,000 tons, if vessels are partly loaded). This step would entail dredging work of a volume of about 350 million cu. meters.

6. While firm estimates of Step 2 are believed to have been developed by SCA, this could vary depending on the additional dredging, navigational and signalling equipment that could be procured as part of this Step, besides the provision of new workshops and berthing and administrative facilities at Port Suez and Port Said which have been badly damaged by the hostilities. The cost could be anywhere between $250-300 million. The dredging costs of Step 3 apparently remain to be firmed up, since the amount of rocks that would be encountered while deepening the Southern section of the Canal beyond 62 feet has to be ascertained. However as a rough order of magnitude, Step 3 could involve an expenditure of another $200-250 million. In other words, besides the cost of about $15-20 million for Step 1, essentially clearance work, the cost of the expansion through Steps 2 and 3 is likely to be of the order of $500-550 million.

II. Traffic for The Expanded Canal

7. Studies that SCA has apparently made on this matter, recognize that the staple source of revenues from the Canal would come from oil tankers transporting Middle Eastern oil to Europe. SCA projects European oil consumption by 1980 to be about 1,100 million tons a year, of which 700 million tons would be supplied by the Middle East. It assumes that by that date, 60 million tons would be carried through the Tapline and the Iraqi Pipelines, leaving 640 million tons to be carried to Europe by oil tankers. Assuming Europe's consumption of Middle Eastern oil to be lower, and transport of oil by pipelines (including the SUMED pipeline to be built by Egypt itself) at a level three times higher, than what SCA projections indicate, Middle East oil carried by tankers to Europe and destinations other than Europe could be of the order of 500 million tons a year by 1980, compared to the 1970 level of about 300 million tons.

8. The essential question is whether with the availability of an expanded Suez Canal, oil companies will find it more economic to use tankers of less than 300,000 dwt which such a Canal could accommodate, or continue the trend towards even larger tankers. SCA has predicated its expansion program on the former premise. SCA's studies indicate that as of June 30, 1970, the world fleet of tankers, 3,049 tankers totalling 138 million tons, included only 6 tankers (totalling 2 million tons) of 300,000 dwt and over. New tankers on order at the time, totalled 496 and 68 million tons, of which only 9 tankers (totalling 3 million tons) were those of 300,000 dwt and over. However as many as 221 tankers on order were between 200,000-300,000 dwt. In other words, over the next few years, tankers over 300,000 dwt are likely to constitute less than 5 percent of the world tanker fleet. It is also not at all clear whether most of the over 300,000 dwt tankers will be used for oil transport from the Middle East to Europe, or for transport of Middle-East oil and Venezuelan oil to Japan and Venezuelan and African oil to USA and Europe. Such tankers might conceivably yield economies for distances involved between the latter regions. Since the distance from the Arabian Gulf to Europe by the Canal is shorter by as much as 5,500 nautical miles than the Cape route, it might be a reasonable assumption that oil companies might find it cheaper to use tankers with dwts less than 300,000 and go through an expanded Suez Canal, and use larger tankers on other routes. Apparently, SCA has also done some studies which suggest that in any event, the cost per ton mile for tankers below 300,000 dwt has an edge over tankers exceeding that tonnage, in view of the higher depreciation, doubling of insurance charges, higher harbour and related dues, etc. that tankers over 300,000 dwt would have to bear. When this factor is related to a substantially shorter Canal route, the economics could favour the use of tankers of a smaller tonnage, particularly if the Suez Canal passage charges are not unduly increased.

9. Obviously the economic justification for the expansion of the Suez Canal will depend on the answers to the questions of the economics of competing alternate systems consisting of various combinations of carriers and routes. One can however surmise that SCA has developed sufficient background data on this aspect, from which such an analysis can be made by the Bank when evaluating the expansion proposal.

10. Together with oil tanker traffic, other vessels carrying goods, ores, etc., are assumed by SCA to be larger in size and tending towards container-carriage. The assumption is that by 1980, total traffic through the Canal is likely to be about 28,500 vessels a year, or a daily average of 78. This compares to a daily traffic of 58 in 1966.

III. Financial Return

11. No specific indication is available as to the financial return calculations that SCA might have made for the Suez Canal expansion proposal. SCA suggests that by 1980, the Canal will cater to a traffic (north and south-bound) close to 1,000 million tons a year. Assuming a more conservative figure of between 600 to 700 million tons a year, and Canal dues of an average of $1 per "Suez Canal net ton" (calculated in accordance with specific rules pertaining to methods for vessel-space and weight measurements), the annual gross revenues could be of the order of $500 million. The average ratio of operating revenues to operating expenses (including depreciation and maintenance) for the Bank-financed 1959 Suez Canal Project, was around 1:.46. Assuming a higher ratio of 1:.50 for the expansion program, the operating income prior to debt service and provision of other fiscal reserves, could be of the order of $250 million annually. Even a lower operating income should yield, after providing for such reserves and debt service on borrowings made for a $550 million investment, a rather attractive profit margin for SCA. The above is obviously a back of the envelope calculation, and would need to be carefully analyzed when the expansion program is considered. However, the financial viability of such a program promises to be attractive.

IV. Conclusion

12. In conclusion, it would seem that the Suez Canal expansion could be handled in the following manner. The immediate clearance and dredging work and purchase of some essential equipment (entailing a possible investment of $15-20 million), which would permit passage of ships with 40 feet draught, could be quickly appraised as a Bank-financed project. Such a project would also allow for a quick disbursal of funds, within 15 to 18 months, to UAR. While this initial project is being implemented, the Bank could assist SCA in developing a thorough economic and financial evaluation of the entire expansion program and settling on the technical details, and could thereafter appraise the program. In view of its magnitude, it might be possible to think in terms of approaching the program in two phases. It might also be recognized that even if the foreign exchange component of the program is as much as 50-60 percent, the counterpart financing requirements would still be rather massive, and its provision could pose some problems for SCA or the Government. Some contribution towards local currency expenditures might therefore need to be considered. In any case, while a significant portion of financing for the program could conceivably be considered by the Bank, on a basis similar to enclave type of projects, we might be able to organize a consortium of interested external donors and international agencies for providing the balance external financing requirements of the program.

ADavar/llj
June 2, 1971

Attachment 1

Middle East Task Force
Briefing for Mr. McNamara

1. In July 1967 it was decided to embark on a number of special, coordinated studies of the development opportunities in the Middle East. The vehicle for carrying out these studies is the Middle East Task Force which includes within its membership all those assigned from time to time to work on the studies. The Task Force's work is steered by a committee composed of representatives from the Projects, Legal, Economics and Middle East and North Africa Departments. Mr. Lejeune acts as Chairman.

2. The aim of the studies is to identify what can be done to accelerate the economic growth of the countries of the region, giving special consideration to those sectors and projects which might contribute to political stability in the area, among which those providing productive employment for the large numbers of unemployed and under-employed, including Arab refugees in the region, will be given special attention. The studies are addressed to the region's overall potentialities and have began with emphasis upon the productive sectors: agriculture, industry and tourism. A broad approach of this kind is consistent with the objective in mind in setting up the Middle East and North Africa Department of taking a new look at the region, and, being wide in scope, is less likely to be looked upon suspiciously by those governments who are prone to be sensitive about their rights to international water and the rights of displaced Arabs.

3. Initially it was hoped that these special studies would discover radical, imaginative projects which could yield quick results in raising living standards and providing work for the unemployed and hence be capable of playing an important part in any peace settlement. Large scale desalinization of sea water for irrigation was one example. Accelerated development of existing fresh water supplies was another. The conclusion was reached fairly quickly as discussed below that great new projects such as might capture the imagination of both potential donors of aid and the people in the recipient countries were not likely to be identified in time to play a part in an early peace negotiation.

Agriculture

4. Efforts were concentrated initially upon opportunities in agriculture, particularly for land and water development. The Projects Department undertook responsibility for this study and began this study using only the information available within the Bank and the U.S. Government. Initial attention was given to the Jordan River Basin, the rest of Jordan, Israel and the Sinai, the Litani and the Tigris-Euphrates River Basins, the Sudan and the possibilities for desalting sea water. While the information available proved inadequate for detailed study, some preliminary findings were possible. They were as follows:

(a) that the land and water resources in the Jordan Valley and in the surrounding areas in Israel, Jordan and south-eastern Syria were unlikely to provide a basis for self-supporting settlement of an important part of the unemployed population; (b) that by irrigation developments based upon the presently unused waters of the Litani River either in Lebanon or in the areas that can be commanded from the Jordan River and from Israel's Main Conduit a somewhat larger, but still not significant, settlement possibility might be provided; political constraints as well as Lebanon's own long-term needs make such developments highly uncertain in any case; (c) that the Israeli Negev, Sinai and the Gaza Strip might offer possibilities at some future date, but that the economics of desalinated water (see below) were such that these possibilities were not realizable within the next ten to fifteen years; (d) that both the Tigris-Euphrates Basin and the Sudan offer possibilities for refugee settlement in agriculture which might be large enough to accommodate a major part of the unemployed and underemployed refugee population; again political constraints made such possibilities entirely dependent upon a general settlement which have to include not only the Arab countries bordering on Israel, but also more distant ones such as Iraq and the Sudan, if they were to be asked to absorb refugees.

5. Preliminary findings with respect to desalted sea water and its use in agricultural production were embodied in two memoranda from the Projects Department dated October 17, 1967, one by Mr. Piccagli and another by Mr. Bell. Based on information available at that time, it seemed doubtful that in the near future desalinated water could be used in agriculture in such a way as to provide a livelihood for settlers even if the capital cost of a dual purpose power and desalinazation plant were a gift. On the other hand, a combination of improved technology and reduced cost (in the desalination process and the supply of heat, i.e. from breeder reactors) with the development of much higher yielding varieties in agriculture, along with much higher skill and management levels in agriculture, might produce a different conclusion sometime in the 1980's. To this preliminary conclusion it should be added that if the capital cost and, to some extent, the operating costs of a desalted water supply project were to be consciously subsidized, the water could be economically used. The question would be whether the amount of money needed for subsidy (or initial grant) might yield more if otherwise invested. With respect to this, one would have to note that the alternative more favorable investment opportunities are very likely to be outside Jordan and the Sinai and, therefore, might be realizable only if substantial numbers of the unemployed could be induced to emigrate; this might be either difficult or undesirable.

Tourism

6. Tourism is largely an undeveloped subject in the Bank Group. Only in the last few weeks has a department - the Projects Department - been given the task of developing it. Just before this decision a prospectus for undertaking the study of tourism in the Middle East was drawn up. Arrangements are being made to have the Bank represented at a meeting of the Middle East members

of the International Union of Official Travel Organizations (IUOTO), scheduled to be held soon in Beirut, to draw up terms of reference for a study of the prospects for tourism in the Middle East to be undertaken by consultants for IUOTO. The IUOTO study, if properly carried out, would provide the first step in a large study to be completed by the Bank, which would aim at the identification of specific investment opportunities in this field.

Industry

7. The possibilities of undertaking studies on industrial development have been under review by the Economics Department in consultation with IFC and the Projects Department, and a prospectus for further studies is under preparation. These would examine industrial policies and prospects, including the role of industrial financing institutions, possibilities for greater regional cooperation in the development of markets and the prospects for better financial and managerial arrangements with outside corporations and investors. An attempt will be made to identify projects of importance in this sector.

Other sectors

8. Attention is also being given to the possibility of using effectively, in the conduct of minor civil works programs, techniques similar to those used in the Comilla Project in East Pakistan. These involved considerable local initiative, combined with high labor and low capital inputs.

9. In connection with the studies in the various sectors the need for trained manpower will be studied, and in relation to this the Projects Department is undertaking a review of the educational and training facilities in the area.

Methods of Investigation

10. The Task Force studies were begun using only information available within the Bank and the U.S. Government, the latter under a special arrangement. During his visit to several countries in the Middle East in November and December 1967, Mr. Lejeune discussed these studies in general terms with the officials he met and arranged to get additional information from them. Subsequently, letters were sent to the Finance Ministers of Iraq, Jordan, Syria and the UAR outlining the information required. Mr. Benjenk discussed this further during his recent visit to Israel and Jordan. The general reaction has been favorable.

11. Meanwhile, various contacts have been made with consulting firms which have carried out major studies in the region and with European governments which have financed such studies. The Kreditanstalt für Wiederaufbau in Frankfurt has compiled a list of major studies financed or carried out by the German Government.

12. The economic missions which have been sent and will be sent to the UAR, Syria and Iraq have been apprised of the need to cover the productive sectors somewhat more thoroughly than is customary in such missions. The first special (two-man) mission for the Task Force has just completed a two-week visit to Jordan, where the members have been gathering information on "wadi" and ground water resources.

13. If the studies are carried out as planned during the next year, it will be necessary to allocate approximately ten man-years of full-time effort to this work and to spend approximately $250,000 for consulting services.

Other Studies

14. After some months of preparation the Ford Foundation is embarking on a series of studies similar to those already begun in the Bank. There has been periodic consultation with a view to coordinating the work and avoiding duplication as much as possible. More recently the U.S. Government has begun its own studies under the direction of a Deputy Assistant Administrator of AID. There have been meetings with the U.S. group to exchange information and report on plans. It appears from these discussions with the Ford Foundation and AID that the studies financed by the Ford Foundation will cover a much broader range of subjects, including political and social questions. It is probable that the AID studies will concentrate on the prospects for nuclear desalinization plants.

Middle East and North Africa Department
April 29, 1968

FORM NO. 57

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

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Attachment 2

~~CONFIDENTIAL~~

OFFICE MEMORANDUM

TO: Mr. Mohamed Shoaib, Vice President

DATE: August 13, 1968

FROM: J. C. Dumoulin JCD

SUBJECT: MIDDLE EAST TASK FORCE: POSITION REPORT

1. Upon your request I have prepared this position report on the Middle East Task Force. It includes information about progress made during the recent months in the three main sectors, namely agriculture, industry and tourism, as well as reports on the contacts the Bank had during this period with the Ford Foundation and the Carnegie Endowment for International Peace, two organizations presently working on surveys related to economic development in the Middle East area.

2. Agriculture: Study of Agricultural Development Potentialities

On February 19, 1968, a memorandum prepared by the Projects Department presented a "tentative plan of study, staff requirements, and required outside assistance" for the agriculture group of the Middle East Task Force. This plan assumed that:

a) "the study would assess the agricultural development potentialities in Jordan, Israel, UAR, Lebanon, Syria and Iraq";

b) "the target date for the first draft of a comprehensive report on the results of the study would be Spring 1969";

For the studies, a sequence of three steps was considered:

a) an inventory of the physical resources and of existing land and water use;

b) systematic identification of potentials and opportunities for agricultural development including alternatives; and

c) formulation of an investment program on the basis of analysis and evaluation of the alternatives.

Provided that adequate personnel, as estimated and required in this plan, could be assigned, it was estimated that steps a) and b) could be completed for all the countries by sometime in the summer of 1968, and step c) by sometime in the spring of 1969.

2.2. On July 29, a memorandum from the Projects Department "reported the present status of the various agricultural sector reviews and proposed an approach designed to accelerate and focus the ongoing efforts." The main elements of this document can be summarized as follows:

a) countries sector reviews: for the UAR, Jordan, Lebanon, Syria and Sudan, draft reports on agricultural development potentialities have been prepared for discussion; in addition, for the same countries and for Iraq and Israel, the main results have been summarized in one brief draft for each country. Except for Jordan, the sector reviews "have had to build on the works of missions geared to the more general requirements of country economic reports." Complaining about the "ambiguous priority status of the Middle East Sector Review" the authors emphasize the constraints which limited the research, and write: "The essential evaluation of existing information in the form of feasibility reports, resource surveys, and marketing studies, which should parallel detailed sector reviews, by and large has not been carried out since the corresponding staff requirements would have exceeded the usual staff allocations for economic missions."

b) regional aspects of agricultural development: in the course of the country-by-country review the authors noted that some problems involving more than one country should be treated regionally. This is particularly the case for two river basin surveys: the use of the waters of the Euphrates River concerns Turkey, Syria and Iraq; in the same way water development in the Nile Basin concerns the Sudan and the UAR. For the Euphrates River a preliminary computer analysis has already been made in cooperation with a Harvard University team and the report has just been published (see below, par. 2.3). Before proceeding the Bank research team now needs new instructions. The authors stress also the fact that "beyond these most obvious regional water development problems," (many other problems, either regional by nature or needing a regional approach) "offer themselves as promising subjects for intensive review."

c) operational implications and proposed approach: given the amount of research, which remains to be done, and which would be required even by the mere realization of the present projections in the Bank's Five-Year Plan, the authors express the need to concentrate their efforts, and ask a clear indication about the relative priority of such work and about its desired focus. They suggest that, for the coming year, they limit themselves to an intensive review of three countries only, namely the U.A.R., Iraq and Jordan and leave aside Lebanon, Israel, Syria and Sudan. Organizationally it is proposed that a review group to carry out this work be constituted as a long-term technical assistance group within the Agriculture Division of the Bank, possibly drawing upon FAO staff. The group, coordinated by a full-time chief and deputy, would consist of two country teams; one for UAR and one for Iraq (Jordan requiring only a subsidiary effort), each of them composed of two economists, one general agriculturist and one irrigation expert. In addition, each team should be able to draw upon the part-time services of a livestock expert and of a marketing specialist.

On this basis and assuming a cooperative arrangement with FAO, it has been estimated that evaluating agriculture in Iraq would require a total of roughly 900 man-days, over a period of 9-10 months at a cost of US$ 115,000. The cost for the review in the UAR being quite similar and taking into account the subsidiary work in Jordan on a one-year basis, the two teams would cost about US$ 300,000. This cost does not include detailed, longer-term studies of river basins or detailed project preparation.

The authors conclude by stating that "their review of the agricultural sectors of the Middle East countries indicate that to meet the operational needs of the Bank, there is no alternative to the kind of systematic approach described above."

2.3. The Euphrates River Basin Survey:

We have already mentioned above progress made by the group working on the Euphrates River Basin survey. Two reasons justify that more information on this survey be given here: a) it is a good example of "evaluation of agricultural development potentialities in a regional context" and as such it fits in very well with the preoccupations of the Middle East Task Force; b) a first phase of the survey has just been carried out, and decisions have to be made now for the next ones.

Here are some elements obtained from the "Systems analysis of the Euphrates River Basin" draft report:

"The use of the waters of the Euphrates River is a vital factor in the economy of the riparian states of Turkey, Syria and Iraq, whether the water is used for domestic purposes, irrigation, power, or the abatement of salinity. Major multipurpose storage developments are going on in Turkey (Keban Dam) and Syria (Taqba Dam), and are planned in Iraq (Haditha Dam)." Of course, availability of water at any point on the course of the river and at any date is dependent on decisions on water use and storage made upstream; the comparison of present and projected water use with mean annual river flow (see table below) shows that all the future projects, presently considered by each of these countries without regional coordination or cooperation, are incompatible:

	Cumulative water use (in $10^9 m^3$)		Mean annual river flow
	present	projected	
Turkey	1.5	15.1	19.9
Turkey + Syria	4.5	24.0	26.1
Turkey + Syria + Iraq	16.2	40.1	28.9

A linear programming model has been built and solved in order to answer the following question:

given: - the time pattern of inflow into the Euphrates basin in a typical year

- the existing regulation capacity of Keban Dam, Taqba Dam and Habbniya Lake (Iraq)

- the hydropower installations at Keban and Taqba

- the existing irrigated areas in Syria and Iraq

- the storage and irrigation development opportunities which have been identified how should the Euphrates system be developed and operated so as to maximize the net benefits from:

- the hydrological resource endowment (as described by the hydrology of the "typical" year)
- the sunk investment (Keban, Taqba, Habbanya, power installations and existing irrigation systems)
- any further investment in the development of the Euphrates system (Haditha Dam and new irrigation projects)

One assumes that all decisions affecting water use and storage in the Basin are made by an unique center; it is equivalent to say that this optimal solution implies a full cooperation of the "players", i.e. of the riparian countries. Any other solution, either non-cooperative or corresponding to a limited cooperation (two out of the three countries, for instance) will be suboptimal and, total benefits will never be superior to those reached by the optimal cooperative solution.

This type of formulation and the solution of the maximization problem indicates not only the optimal use of water in the basin, i.e. the one leading to the largest benefits, but also the "costs" of the constraints, i.e., the extra benefits obtainable by relaxing them. One can also compare this optimal solution to suboptimal solutions resulting from different degrees of cooperation between the riparian countries, and deduce their bargaining power: these results are absolutely essential if an external authority, such as the Bank, wishes to assist the riparian countries in establishing a "fair" agreement leading to an optimal allocation of resources (land and water) in the area.

It is not necessary to detail here the results of this first analysis. The author emphasizes the fact that "the findings have to be understood with reference to the analytical framework within which they were obtained. Thus, the results are only valid to the extent that the model captures the strategic aspects of the Euphrates system." In particular, the model is still static and deterministic; "it does not capture those aspects of systems planning and operation which are designed to cope with hydrological variability and uncertainty." Part of the quantitative data included in the model are also provisional and will be revised. "Nevertheless, the model as described above was a useful first step in the direction of a comprehensive analysis of the system."

Eventually the author recommends the following program for the next months:

step 1: detailed review of all available information about the hydrology, and past operations pattern of the Euphrates system; mainly in Iraq, but partly also in Syria;

step 2: analysis of the impact of Keban dam upon the operation of the system;

step 3: detailed review of all irrigation development opportunities whether they involve intensification of irrigated cultivation in existing project area or expansion of irrigated area;

step 4: analysis of the impact of Tabqa Dam upon a system which is already substantially regulated by Keban Dam.

No estimates have yet been made of the cost and duration of this new part of the survey.

2.4. Nuclear Desalting Plants:

No new specific development concerning this type of project is worth noticing inside the Bank. The preliminary conclusion reached in October 1967 when Mr. Piccagli and Mr. Bell studied sea-water desalination and the use of desalinated water in agricultural production, still holds: "it is doubtful if desalted water can be produced at a cost low enough for use in agriculture before the 1980's at the earliest without very substantial subsidies covering more than total capital costs." On the other hand, the Bank went on keeping contacts with persons and organizations interested in that field: on June 26, Mr. E. deRothschild visited Mr. McNamara and presented to him his "Plan for Raising Living Standards in the Middle East." Mr. McNamara exposed the point of view of the Bank, and said that it was impossible for the Bank itself to undertake to finance such proposals that imply a heavy subsidy. He expressed also his opinion that, under favorable political circumstances, and if the governments or combination of governments subsidizing such a project wished it to do so, the Bank would be prepared to consider playing the role of managing agent for a project of this type. In May, Mr. Ionides, a British authority on Middle East water problems and Mr. Doxiadis visited Mr. Lejeune and spoke with him to offer their service to the Bank if the Bank should come to the stage of employing outside consultants for a study of water resources in the Middle East. They consider a political agreement between the two groups of countries interested in the area to be a prerequisite condition prior to any attempt; they support also a very broad approach as well for the area concerned as for the type of solution envisaged which should not be limited to any specific technique as desalination for instance.

3. Industry:

3.1. For some time now, the Economics Department has been working on a survey of industry in the Middle East area. On June 29, a meeting was held to discuss Mr. B. de Vries's paper of June 17, which described the objectives of the survey in the following terms:

"The survey should undertake to examine:

a) industrial development strategy, major prospects in specific and complementarity and coordination of economic policies;

b) industrial policies, including protection policies, management and finance, and financing arrangements for small industry; and

c) adjustments and benefits implied by possible schemes of regional cooperation."

3.2. Three countries -- Syria, U.A.R. and Iraq -- have already been visited; Lebanon, Saudi Arabia, Kuwait, Jordan and the Gulf States will also be included. During the meeting it was also agreed that Israel should be put on the list, and also Tunisia, Lybia and Sudan because of the special interest these latter countries present for a survey of socialized industry and public enterprises.

3.3. It was also agreed that "the study would be related to the Bank's operational interests. This does not mean that in all cases it would be confined to countries where the Bank group will finance industry. In some cases, it may involve discouragement of excessive industrialization and encouragement of more efficient industrialization."

3.4. Three country surveys has been published on U.A.R., Syria and Iraq, which will now be reviewed. A note will also be ready in the first days of September, giving cuntry by country, a brief summary of the main characteristics of industry (present situation by sectors, endowments in natural resources, skilled labor, etc., - potentials and particular advantages in the framework of a regional approach) and a more detailed, regional survey in two sectors: fertilizers, and engineering.

4. <u>Tourism:</u>

Mr. H. D. Davis, from the Projects Department, attended an IUOTO meeting in Cairo (July 15-18) as an observer to explore the degree of Bank involvment that might be warranted, in a proposed study of the prospects for tourism development in the Middle East. Seven countries attended the meeting: Jordan, Syria, Iraq, UAR, Kuwait, Lebanon and the Peoples Republic of Southern Yemen (Aden), as well as the Secretary General of IUOTO and representative of the prospective consultants (Transport and Tourism Technicians Ltd., of London).

It was agreed that the study should go forward and a "Specification" for it produced by IUOTO, according to which:

"The general objective is to study the ways and means by which the area comprising the seven member countries could be developed in order to make the optimum use of its tourism resources so as to maximise the economic and social benefits it can derive from tourism."

The following main aspects will be covered:

- Forecasts of the potential tourist trade of the area
- Conclusions on the relative appeal of the tourist attractions of the area to the world's markets, and on ways in which the appeal of some of these attractions could be enhanced by their coordinated development and promotion.

-Evaluation of the tourism plant necessary.

-Recommendations on the co-ordinated marketing policies and practices.

-Estimates of the potential revenues to the area.

-Recommendations for inter-countries collaboration.

The area covered is limited to the seven member countries and the survey will be based primarily on the assumption of the restoration of the geographical situation prior to the events of June 1967, but will "also consider the negative effect which would result from a continuation of the present situation."

It is considered that Bank intervention and support of this study would be useful and would ensure that it more closely met Bank's requirements. IUOTO is prepared to allow the Bank to participate in the study, to receive information and to comment at each stage. If the Bank were involved, the total cost of the study would be $75,000; the cost to the Bank could be expected to be in the order of $20,000 (one-third of fees to consultants and a $5,000 participation to IUOTO overhead cost).

5. Contacts:

The Bank has been informed of two surveys concerning the Middle East area, conducted for the Ford Foundation and the Carnegie Endowment for International Peace.

The Rand Corporation, together with Resources for the Future, is doing a major research project for the Ford Foundation on economic and political aspects of the Middle East. Sidney Alexander, an economist from MIT is working with the Rand Corporation, as research director of the study. The study's objectives are to help Ford obtain a better basis for planning its operation in the Mid-East and to determine feasible alternatives, if any for economic development in the region considering political realities. The survey will cover the area located between Morocco and Iran with particular emphasis on the area from Egypt through Iraq. Reports will be produced next summer and will be available for the Bank. Meanwhile, contacts and exchange of information will be maintained between Bank staff members and the two organizations in charge of the survey, as it has been the case during these last months.

Another survey is to be undertaken under the aegis of the Carnegie Endowment for International Peace: "The Settlement of the Middle East Refugees: Proposed Economic Survey." The Survey is to be carried out under the full-time direction of an "outstanding international civil servant" which could be Sir Eric Wyndham White. In May, Mr. Harris, one of the Vice-Presidents of the Carnegie Endowment met with Mr. Lejeune, who later received also Sir Eric Wyndham White. (This visit followed contacts between Mr. Friedmann and Senator Javits). After being informed on the research made in the Bank on the same problems, Sir Eric asked whether people in the Bank would be willing to contribute ideas and comments to those working on the Survey and Mr. Lejeune answered positively. At that time Professor Wilson of Indiana University was approached to undertake the first part of the survey, i.e. pulling together basic data and plan the survey. No new information on the progress of this work has been recently transmitted to the Bank.

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MIDDLE EAST

At the meeting of the Executive Committee of the Commission on the Middle East in Washington on 25 August 1970, it was decided that the most useful role the Commission could play would be to prepare a development plan that would take into account the social and economic needs of the Palestinian Arabs and be of assistance to the UN Mediator in carrying out his negotiations.

Ambassador Velebit submitted to the Executive Committee on 3 November 1970 a report entitled "Proposal for the Preparation of a Blue Print for Economic and Social Development in Jordan, the Lebanon and the Part of Palestine under Israeli Military Administration." The report and the budget of $250,000 were approved. Subsequently, the budget was approved by the Carnegie Endowment Trustees at their meeting on 23 November 1970.

Since that time Ambassador Velebit has been involved in efforts to put together two teams of economists and other appropriate social scientists, which would have the task of preparing development programs for the Arab and Israeli sectors of greatest unemployment.

At the end of March 1971 an agreement was approved by the Executive Committee of the Commission and signed by Ambassador Velebit with the Israel Institute of Applied Social Research to prepare a development plan for the West Bank and Gaza Strip. The study will consist of:

a) A model of a development program, under alternative political assumptions, which will give priority to the creation of gainful employment, both short and long term, for the manpower of the area covered, and which will establish employment targets by area and by economic sector.

b) Suggestions for projects, directly productive, as well as intrastructure investment, to achieve the suggested employment targets.

c) An indication of the legislative measures and an estimate of the financial costs required to implement such projects. The cost estimates should cover the amount and character of external and internal financial requirements, covering a period of 5 and 10 years, respectively, and taking account of the absorptive capacity of the area.

d) A statement of the development objectives and of criteria for the evaluation of the suggested projects, on the basis of which priorities could be established.

The study is scheduled for completion no later than 31 August 1971.

Ambassador Velebit is now involved in negotiations with two Yugoslavian Institutes for a parallel study on the Arab side. He has been assisted in the negotiations and the research design by the economist, Professor Richard Gilbert, formerly with the Center for International Affairs, Harvard Development Advisory Service.

Attachment 3

Middle East Studies

A. Studies by the Bank

Little research was done by the Bank itself. Apart from our regular economic reports on middle-eastern countries (UAR, Israel, Jordan, Lebanon, Syria and Iraq) only one study was prepared by the Bank's staff:

1. R. Sadove, Middle East: Agricultural Sector Reviews, July 29, 1968.

   Two other studies were initiated by the Bank but undertaken by outside consultants:

2. Computer Analysis of the Euphrates River System, 1968.
3. IUOTO, Prospects for Tourism Development in the Middle East Region (draft), Geneva, December 1970.

B. Consultants Reports made available to the Bank

1. The Yarmouk-Jordan Valley Project. Harza Engineering. March, 1962.
2. East Bank Jordan Water Resources. Hunting Technical Services and Sir M. MacDonald, 1965.
3. Planning for the Development of the Jordan River Basin by President Johnson's Middle East Task Force. June, 1967.
4. Jordan Valley Project by Dar-Al Handasah (Beirut) and The Netherlands Engineering of the Hague. December, 1967.
5. Kerak-Hasa Groundwater Irrigation Project. Sir M. MacDonald and Partners and Hunting Technical Services. October, 1968.
6. Israel Water Development Program 65-80, Tahal, 1964.
7. For U.S.-Israel Joint Board: Engineering feasibility and Economic Study for Dual Purpose Electric Power. Water Desalting Plant for Israel. January, 1966 (Kaiser Engineers and Catalytic Construction Company).

8. The Engineering Economics of a large-scale desalting plant in Israel (Paul W. MacAvoy - MIT and Dean Peterson of Utah State University), February 15, 1967.

9. An agro-economic and a socio-economic evaluation of the Euphrates project by Nedeco for Euphrates Project Authority. Syria, August, 1964.

10. Hydrological survey of Iraq by Harza Engineering Company and Binnie and Partners for the Government of Iraq. 1963. (NESA)

11. Studies of Development on the River Diyala by Tom Jewitt, of Hunting Technical Services. October 6, 1967. (Memo V.C. Robertson to Sadove).

C. Rand Corporation: Resources for the Future /1

1. Middle East oil and the Western World by Homan et al Schurr July 1969 (draft).

2. Economic Development and Population Growth in the Middle East by Cooper and Alexander - to be issued September 1971.

3. Regional Arab Politics and the Conflict with Israel by Malcolm H. Kerr - October 1969.

4. United States policy in the Middle East: Constraints and Choices by William B. Quandt - February 1970.

5. Meteorological Aspects of Middle East Water Supply by R.E. Huschke, R.R. Rapp and C. Schutz - March 1970.

6. Fertility patterns and their determinants in the Arab Middle East by T. Paul Schultz - May 1970.

7. Changing Military perspectives in the Middle East by J.C. Hurwitz - September 1970.

8. The Agricultural Potential of the Middle East by Clawson, Landsberg and Alexander, 1971.

/1 Financed by Ford Foundation

THE SECRETARY-GENERAL

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24 May 1971

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Dear Mr. McNamara,

I enclose copy of a letter dated 9 May from His Majesty King Hussein of Jordan which was brought to me by the Permanent Representative of Jordan to the United Nations on Friday 21 May.

I would like to discuss the proposal contained in this letter with you and with my concerned colleagues at the United Nations (Messrs. de Seynes, Hoffman and Narasimhan) at a convenient date fairly soon. My office will be in touch with your office to arrange a mutually convenient date and time.

With kind regards,

Yours sincerely,

U Thant

Mr. Robert S. McNamara
President
International Bank for Reconstruction and Development
1818 H Street, N.W.
Washington, D.C. 20433

President has seen

THE ROYAL PALACE,
Amman, Jordan,
May 9th, 1971.

Dear Friend,

As you will know Mr. Secretary General, the situation in this area of the Middle East is still critical and potentially dangerous to those who live in it, and to the world at large. However, hopes have not been completely relinquished that a just and thus lasting peace might be achieved, in the interest of all in the area and the world community, through the implementation of Security Council Resolution Number 242 of November 22, 1967, and the establishment of all the principles it contains.

Looking with optimism towards such an end, I feel it necessary at this stage to solicit your help, possibly in cooperation with the World Bank on a subject that does not affect Jordan alone, but the area as a whole: This is the carrying out of an economic study of the Middle East with a view to proposing a regional development programme which could be implemented once peace is reached. We realize that such a study would be time and effort consuming, but at the same time we feel it would be well worthwhile if and when peace and stability prevail in the area.

Your Sincere Friend

Hussein I.

His Excellency
U. Thant,
Secretary General,
United Nation,
New York City, N.Y.,
U.S.A.

THE LIQUIDITY CRISIS

1. The liquidity crisis, in which Pakistan now finds itself, has been the combined effect of two factors. First, beginning in 1969/70 and continuing through December 1970, import licenses were issued and other payments authorized in amounts far in excess of available exchange resources. In the climate of speculation against the exchange rate that prevailed, available licenses were taken up quickly and orders placed against them. Excess authorizations, combined with speculative pressures, resulted in Pakistan losing, in the current financial year, exchange assets at an average monthly rate of roughly US $15 million, for a total of US $134 million from July 1, 1970 through March 31, 1971. 1/ Second, exports from East Pakistan were suspended at the beginning of March and no shipments took place through the end of April. Consequently, in May and June Pakistan will not receive exchange earnings in the order of US $25-30 million a month which normally would have accrued. Thus, what was already a difficult exchange situation was greatly exacerbated by the suspension of economic activity in the East Wing.

2. It is difficult to see any possibility for the Government, through action in the economic or financial sphere, to avert bankruptcy. Whether Pakistan will in fact run out of exchange reserves over the next few months or whether it will just pull through will be determined by the relative movements in outstanding payments commitments falling due and in export earnings from East Pakistan. On the payments side, commitments, in the form of letters of credit for imports, in the order of US $250 million were outstanding at the end of April. As for exports from East Pakistan, some small shipments of jute are reported to have been made in early May. However, these were from stocks already at Chalna, the major port for jute exports; total stocks there and at Chittagong are estimated at only 25,000 tons, having an export value of roughly US $6 million. Thus, resumption of jute exports in significant quantities would depend on trade and distribution links with up-country areas being restored.

3. As of April 29, 1971, Pakistan's official holdings of exchange assets in convertible currency 2/ stood at US $137.6 million. At this level they were US $9 million more than a month earlier. This increase cannot, however, be taken as an indication of an improvement in the underlying trend.

1/ Including the use of SDR's.

2/ Comprising US $67.2 million in foreign exchange, US $16.9 million in SDR's, and US $53.5 million in gold; excluding assets of US $25 million that represent the counterpart of deposits by foreign banks.

It appears rather to have been the result of several special factors: First, exports of jute and jute manufactures in February, the proceeds of which Pakistan would receive in April, were, at US $32 million, about 20 percent above the monthly average obtained in the first 7 months of the current fiscal year. Second, about US $6 million was received from Mainland China as an installment towards the purchase of planes from Pakistan. Third, from February onwards strong efforts were made by the authorities to reduce the amount of claims outstanding against aid-giving countries and institutions under reimbursing arrangements. Fourth, because of an error in communications between the Government and the State Bank, all debt service payments were suspended on April 13; the error was only detected towards the end of the month, and out of total payments of US $22 million due in April a substantial portion probably slipped into May. It is impossible to put a precise figure on the combined effect of these special factors, but US $20-30 million appears to be a reasonable estimate. Correction for the deferment of debt service payments would reduce exchange assets held at the end of April by, say, US $10 million to US $127.6 million.

4. To assess the short-term outlook for its reserve position, the Government of Pakistan has prepared a forecast of the balance of payments covering the five months May through September. This suggests that over the period as a whole Pakistan stands to lose US $162 million in exchange assets. Suspension of conversion rights on certain debt payments, as already announced by the Government, would reduce the reserve loss by US $54 million to US $108 million. Thus, according to this forecast, the State Bank would, by the end of September, be left with about US $20 million of exchange assets in convertible currency.

5. Briefly, the assumptions underlying the Government's forecast are as follows:

(a) Receipts - As regards merchandise exports, it is assumed that exchange receipts follow shipments by two months. Thus, receipts in the period May to September represent export shipments in March through July. These are projected as shown below, together with some comparative data (in US $ million):

	Total		Monthly Averages			
	March - July		July - February		March - July	
	1971	1970	1970/71	1969/70	1971	1970
West Pakistan	172	163	32	27	34	33
East Pakistan	67 1/	143	28	29	22 1/	27 1/
Subtotal	239	306	60	56	56	60
Less Barter (10%)	24	31				
Total	215	275				

1/ May-July only.

In the projection of exports from West Pakistan, the weak spot lies in the assumption that in the period April through July the expected seasonal decline in traditional exports (mainly cotton and cotton manufactures) will be offset partly by a rise of 10 percent in other exports. However, altogether the estimated exports from West Pakistan seems reasonable, provided the general economic climate remains conducive to maintaining the pace of export expansion achieved in the first eight months of the current financial year.

In contrast, there is at the moment no factual basis on which to judge whether the projected exports from East Pakistan are likely to materialize. As shown in the table above, the Pakistan Government estimates these exports to average US $22 million a month during the three-month period, May to July, as compared to actual shipments worth US $27 million a month during the same period last year -- the difference in total exports during the two periods being roughly equivalent to the loss of one-half month's shipments at last year's rate. Barring destruction of stocks on a large scale, supplies of raw jute in East Pakistan should be amply sufficient for shipments at the projected rate. Furthermore, achievement of this rate would not depend critically on jute mills resuming full production during the period as more raw jute would be shipped to offset shortfalls in manufactures -- although, of course, such a shift would result in total exchange earnings from the 1970/71 jute crop being reduced. However, critical to the Government's estimate is the assumption that trade and distribution links will be normalized promptly, because, as noted above, stocks available at the points of export are very small. At the moment, it is not possible independently to assess the prospects of normalization proceeding as fast as would be necessary for the Government's estimate to be met.

In addition to merchandise exports, the Government expects Pakistan to have invisible earnings of US $63 million during the period May-September, equivalent to a monthly rate of US $12.6 million. This compares with actual receipts of US $17.9 million a month in 1969/70 and US $14.7 million in the first eight months of the current financial year. As in the case of merchandise exports, two major assumptions underlie this projection: First, that no adverse developments will occur in West Pakistan that would affect earnings, including home remittances, flowing into that wing; second, that conditions in East Pakistan will fast return to normal. Failure of either one of these assumptions to materialize would be reflected in a shortfall below the forecast, more seriously so in the case of West Pakistan which receives the bulk of invisible earnings, including home remittances.

Altogether, therefore, the Government forecasts earnings in convertible exchange to total US $280 million during the period May-September. It expects to receive a further amount of US $15 million by reducing its outstanding claims against aid-giving countries and institutions under reimbursement arrangements. Thus, total expected receipts come to US $295 million.

(b) Payments - The Government's forecast contains separate estimates for merchandise imports (excluding imports under aid or barter), invisibles and debt service payments.

Payments for merchandise imports during the five-month period, from May to September, are projected at US $255 million. Of this amount, US $200 million represents payments against letters of credit already outstanding at the end of April, assuming that 80 percent of such commitments, totalling US $250 million, will fall due before the end of September. The Government assumes that in addition US $55 million will have to be paid during the period against letters of credit opened in May and June, equivalent to 75 percent of new licenses to be issued during these two months.

According to the Government's forecast, payments for merchandise imports would run at a monthly rate about 20 percent higher than during the second half of 1969 and 10 percent lower than in the latter half of 1970. Thus, for a country suffering from acute exchange stringency, imports are projected to continue at quite a high level. One needs to recognize, of course, that the bulk of payments is due on commitments under letters of credit opened some time ago, about which the Government can do little, except perhaps by large-scale cancellation of orders already placed. As for new commitments, the forecast assumes that licenses will be issued for US $75 million in May and June. This would be equivalent to an annual rate of imports of US $450 million, roughly equal to actual imports, similarly defined, in 1969/70 and somewhat above the average level in the three preceding years.

Invisible payments are projected at a monthly rate of US $14 million for the public sector and of US $8 million for the private sector, for a total of US $111 million for the five-month period. At this amount, invisible payments would run at a level somewhat lower than in 1969/70, reflecting, apart from a general squeeze being applied now, mainly savings in freight for fertilizer, reductions in expenditures by officials and missions abroad, and the transfer of certain payments to full bonus. However, this estimate excludes exchange payments for military purposes.

Projected debt service obligations in convertible currency and estimated actual payments, taking into account the suspension of conversion rights on certain debts, are summarized in the table below:

Debt Service Obligations in Convertible Currency
May 1 - September 30, 1971
(US$ million)

Consortium Countries and Switzerland		50.8
International Agencies and Assistance from Consortium Countries outside Consortium Arrangements		35.1
Non-Consortium Sources, including Socialist Countries		4.6
Total		90.5
Debt Service Payments with Deferred Conversion		55.4
of which:	Consortium	49.6
	Switzerland	1.2
	Non-Consortium Sources	4.6
Debt Service Payments in Foreign Exchange		35.1
of which:	International Agencies	19.2
	Consortium Countries	15.9

6. Thus, the Government's forecast of receipts and payments in convertible currency during the five-month period from May to September, may be summarized as follows (in US $ million):

Receipts:	Merchandise Exports		215
	Invisibles		63
	Reimbursements		15
		Total	293
Payments:	Merchandise Imports		255
	Invisibles		111
	Debt Service		35
		Total	401
Deficit			108

In short, according to the Government's forecast official exchange assets would be drawn down during the period by US $108 million, from US $127.6 million 1/ at the end of April to about US $20 million by the end of September, 1971.

7. This conclusion requires some further comment. First, it appears that the Government's forecast excludes payments for military imports. As it is, Pakistan's exchange assets provide only a very small margin of safety as against the estimated deficit. There is no reliable information about the normal current size of military imports, and it is not known what, if any, additional exchange outlays are involved in the armed intervention in East Pakistan. However, if, as seems to be the generally accepted estimate, military imports are normally running at an annual level around US $100 million, outlays involved during the period covered by the forecast would exceed the amount of exchange assets estimated to be left at the end of September.

8. Second, a crucial element in the Government's forecast is the assumption that exports from East Pakistan will quickly be brought back to normal, starting sometime during the month of May. This is so because the bulk of East Pakistan's exchange earnings goes towards financing payments of the Central Government and West Pakistan rather than imports direct to the East Wing. As noted several times before, it is difficult to judge whether this assumption in the Government's forecast is realistic.

9. Third, in view of the very small safety margin afforded by the present level of officially held exchange assets, it is not only the aggregate deficit that is important, but also its distribution over time during the period through September. One important element in this respect is the pace at which exports from East Pakistan are resumed. The other important element is the maturity structure of the letters of credit outstanding at the end of April which amount to US $250 million. The Pakistan authorities have been unable to provide any information about the monthly rate at which these letters of credit are likely to fall due. However, several considerations would suggest that the bulk of these outstanding commitments will fall due in the early, rather than the later, part of the period: in January, a much more restrictive import policy was introduced; between January and the end of March, the value of licenses issued for private imports against convertible currency came to only US $66 million and the total, including public sector imports, may amount to US $80 million; after the introduction of the new import policy there were the usual delays before the new system functioned, which make it unlikely that all the licenses issued through March led to letters of credit being opened by the end of April.

10. In the attached tables, two alternative time patterns are shown for exchange earnings from East Pakistan and for import payments, without altering the magnitudes assumed in the Government's forecast for the period as a whole. They demonstrate how vulnerable Pakistan's exchange position will be

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1/ See paragraph 3.

over the next two to three months to minor departures from the most favorable assumptions. Furthermore, they suggest that the reserve position may well become critical in July. However, it should be noted especially that all these projections assume that Pakistan importers will continue to obtain normal commercial credit facilities for the financing of imports. If this assumption turned out to be incorrect, the situation would be considerably worse than shown in this note.

Attachment

Receipts and Payments
(US$ million)

First Alternative (Early restoration of exports from East Pakistan; even distribution of import payments)

	May	June	July	August	September	Total
Receipts						
Merchandise						
W.Pakistan	39	33	33	33	34	172
E.Pakistan	-	-	19	24	24	67
Subtotal	39	33	52	57	58	239
Less Barter (10%)	4	3	5	6	6	24
Total	35	30	47	51	52	215
Invisibles	13	12	13	12	13	63
Re-imbursements	3	3	3	3	3	15
Grand Total	51	45	63	66	68	293
Payments						
Merchandise	51	51	51	51	51	255
Invisibles	22	22	22	22	23	111
Debt Service	7	6	10	3	9	35
Grand Total	80	79	83	76	83	401
Deficit (-)	-29	-34	-20	-10	-15	-108
Exchange Assets						
at beginning	128	99	65	45	35	128
at end	99	65	45	35	20	20

Second Alternative (Only marginal exports from East Pakistan in May, 70 percent of all payments for merchandise imports estimated to be payable during the period, fall due in May-July)

	May	June	July	August	September	Total
Receipts						
Merchandise						
W.Pakistan	39	33	33	33	34	172
E.Pakistan	-	-	5	31	31	67
Subtotal	39	33	38	64	65	239
Less Barter (10%)	4	3	4	6	7	24
Total	35	30	34	58	58	215
Invisibles	13	12	13	12	13	63
Re-imbursements	3	3	3	3	3	15
Grand Total	51	45	50	73	74	293
Payments						
Merchandise	60	60	60	38	37	255
Invisibles	22	22	22	22	23	111
Debt Service	7	6	10	3	9	35
Grand Total	89	88	92	63	69	401
Deficit (-)	-38	-43	-42	10	5	-108
Exchange Assets						
at beginning	128	90	47	5	15	128
at end	90	47	5	15	20	20

THE EXTERNAL FINANCING PROBLEM

IN 1971/1972

1. In order to illustrate the problems which Pakistan is likely to encounter in 1971/72 in the way of financing imports to support the country's economic activity, a very rough, tentative projection of sources and uses of foreign exchange has been made. The conclusion, based on assumptions about exports that must be regarded as highly optimistic, is that the performance of Pakistan's economy - being critically dependent upon the flow of raw material and other imports - is likely to be seriously affected by the continued interruption in new non-project aid commitments.

2. Exports from Pakistan are projected to increase somewhat to US$714 million which, together with some US$210 million in invisible receipts gives a total of US$924 million in foreign exchange earnings in FY 1971/72. The projection as regards East Pakistan exports is clearly based on most optimistic assumptions. Against these earnings are claims to cover service on existing external debt (US$242 million), invisible imports and defense (US$315 million), and a little over US$100 million to replenish the low level of Pakistan's foreign exchange reserves.

3. Only US$260 million is left to cover imports other than invisibles, capital goods financed under project aid, and military imports. To this must be added some US$150 million for disbursements under non-project assistance already committed. The total comes to US$410 million.

4. Recent estimates of the rice and wheat crop in West Pakistan suggest that there will be a need to import some 500,000 tons of foodgrain into that Wing. In addition, some 2 million tons of foodgrain imports are likely to be required for East Pakistan. Thus total foodgrain imports into Pakistan of some 2.5 million tons may be needed which would cost about US$200 million.

5. On the basis of these estimates, there would only be about US$200 million left to finance imports of consumer goods other than food and of raw materials in 1971/72. In the years 1968/69 and 1969/70 imports of raw materials and consumer goods amounted to some $580 million, indicating - against these totals - a shortfall of some US$370 million for the year 1971/1972.

6. Even after allowance is made for possible reductions in the use of exchange for invisibles, including in particular defense, and imports of consumer goods other than food, the magnitude of the shortfall that emerges from these illustrative calculations is clearly such that Pakistan could not possibly hope to be able to avoid a sharp reduction in economic activity unless it obtains very substantial new commitments of external assistance other than project aid. To the extent that export earnings are less than indicated here - as they would

be unless the economy of East Pakistan functioned normally throughout the year - the situation would of course be that much worse.

7. All this adds up to saying that, if a sharp reduction in economic activity is to be avoided in 1971/72 - and it is obviously meaningless in the present context to think in terms of growth and development - external assistance in the order of US$500 million appears to be needed soon in order to sustain the flow of raw material imports and replenish the pipeline of non-project aid. Of this amount, perhaps US$175 million may be needed in a form equivalent to cash (such as use of the Fund's resources and debt relief), US$200 million in food aid and the rest in non-project aid.

PAKISTAN: SOURCES AND USES OF FOREIGN EXCHANGE
(US$ MILLION)

	1968-69	1969-70	1970-71	1971-72
1. Sources				
Merchandise Exports	681	687	N.A.	714
West Pakistan	357	338		378
East Pakistan	324	349		336
Invisibles	201	249		210
Total Available	882	936		924
2. Uses				
External Debt Service	149	196		242
Invisible Imports, including Defense	207	227		315
Changes in Foreign Exchange Reserves	63	-32		105
Total Uses	419	391		662
3. Available for Financing of Visible Imports	463	555		262
Add: Disbursements from Pipeline of Committed Non-Project Aid	174	193		150
Total	647	748		412
4. Estimated Need for Foodgrain Imports	45	70		200
Net Available	602	678		212
5. Raw Materials Imports	448	480		
Consumer Goods Imports (excluding foodgrains)	123	109		
Total	571	589		

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Files May 17, 1971

J. Burke Knapp (Signed) J. Burke Knapp

Discussion in Ottawa Regarding Pakistan

During my visit to Ottawa on Friday, May 14 Mr. Mitchell Sharp, Secretary of State for External Affairs, asked me to call upon him to discuss the situation in Pakistan.

I gave him a full and frank account of our view of the situation, covering the information derived from Mr. Cargill's visit to Pakistan last week and from the discussions with Muzaffar M. Ahmad in Washington.

Sharp was intensely interested and grateful for the information. He did not give me much of a lead regarding Canada's attitude except that they were very troubled about providing aid to East or West Pakistan before some further developments in the direction of a political reconciliation between the East and the West. (He did not allude to it, but I learned that a special problem had been created for them by the recent espousal of the East Pakistan cause by some of the separatist elements in Quebec.)

I also took the occasion to thank Sharp (as I had thanked Simon Reisman, Deputy Minister of Finance) for Canada's helpful response to our appeal for advance contributions to IDA.

cc: Mr. McNamara ✓
Sir Denis Rickett
Mr. Cargill

JBKnapp:jk

489/3/4

Mr. M. P. J. Lynch

Gregory B. Votaw

PAKISTAN

May 14, 1971

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S E C R E T

I would appreciate it very much if you would kindly transmit the following secret message from Mr. McNamara to Mr. Watanabe, President of the Asian Development Bank in Manila:

URGENT AND MOST CONFIDENTIAL FOR PRESIDENT WATANABE ASIAN DEVELOPMENT BANK FROM MCNAMARA PRESIDENT WORLD BANK

THANKS YOURCABLE MAY 11 STOP BANK STAFF PRESENTLY PREPARING POSITION PAPER TAKING INTO ACCOUNT CARGILL'S VISIT TO ISLAMABAD AND TALKS OF M.M. AHMAD (ECONOMIC ADVISER TO PAKISTAN PRESIDENT) IN WASHINGTON THIS WEEK WITH FUND COMMA BANK COMMA AND US GOVERNMENT STOP PAPER EXPECTED READY FOR DISPATCH MIDDLE OF NEXT WEEK STOP WILL SEND YOU COPY OF PAPER IMMEDIATELY STOP MEANWHILE IT HAS BEEN CLARIFIED THAT ALPHA BANK/IDA WILL CONTINUE TO RECEIVE DEBT SERVICE PAYMENTS BETA MORATORIUM APPLIES TO COMMERCIAL DEBT TO CONSORTIUM COUNTRIES ONLY INSOFAR AS COMMERCIAL CREDITS WERE INCLUDED IN CONSORTIUM PLEDGES OF RESPECTIVE COUNTRIES PARA

LEAVING ASIDE QUESTION OF POLITICAL SETTLEMENT AND ARRANGEMENTS WITH UNITED NATIONS FOR RELIEF TO PREVENT WIDESPREAD FAMINE IN EAST PAKISTAN BOTH OF WHICH I CONSIDER CRUCIAL TO ABILITY OF GOVERNMENTS AND INSTITUTIONS TO RESPOND TO PAKISTAN'S NEED FOR EXTERNAL ASSISTANCE COMMA THE FOLLOWING ARRANGEMENTS HAVE BEEN AGREED WITH M.M. AHMAD FOR RESOLUTION OF ECONOMIC AND FINANCIAL PROBLEMS THROUGH APPROPRIATE REFORM PACKAGE INVOLVING IN PARTICULAR EXCHANGE AND REVENUE SYSTEMS COLON PRIMO A FUND MISSION ACCOMPANIED BY BANK STAFF WILL VISIT ISLAMABAD IN JUNE FOR COMPREHENSIVE REVIEW OF ECONOMIC SITUATION AND DISCUSSIONS OF APPROPRIATE PACKAGE OF MEASURES FOR REFORM OF EXCHANGE SYSTEM STOP SECUNDO FUND MISSION WILL BE PRECEDED BY BANK MISSION ACCOMPANIED BY FUND STAFF TO EAST PAKISTAN TO ASSESS OUTLOOK FOR NORMALIZATION OF ECONOMIC SITUATION AND FUNCTIONING OF PROVINCIAL AND LOCAL ADMINISTRATION AND RELATED BALANCE OF PAYMENTS AND FISCAL OUTLOOK STOP SUBJECT TO CONFIRMATION BY GOVERNMENT BANK MISSION TO EAST PAKISTAN WILL START WORK ABOUT JUNE ONE AND FUND MISSION IN ISLAMABAD ABOUT JUNE TEN STOP BOTH MISSIONS EXPECTED COMPLETE WORK BY JUNE 18 OR 19 STOP A MEETING OF HEADS OF DELEGATIONS PAKISTAN CONSORTIUM IN PARIS JUNE 21 UNDER CONSIDERATION STOP CARGILL WILL CONFIRM DATE FOR PARIS MEETING TO ENABLE ASIANBANK REPRESENTATIVE ATTEND REGARDS SINCERELY

MC NAMARA

Thank you very much for your assistance.

MHW/lgl

489/3/3

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Mr. M. P. J. Lynch

FROM: Gregory B. Votaw

SUBJECT: PAKISTAN

DATE: May 6, 1971

S E C R E T

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You have kindly offered to transmit a secret message from Mr. McNamara to Mr. Watanabe in Manila. This is the text:

"URGENT AND MOST CONFIDENTIAL FOR PRESIDENT WATANABE FROM MCNAMARA PRESIDENT WORLD BANK STOP

IN RESPONSE TO YOUR INQUIRY REGARDING PAKISTAN AM PLEASED TO PROVIDE FOLLOWING INFORMATION COLON PAKISTAN GOVERNMENT HAS NOTIFIED GOVERNMENTS REPRESENTED IN CONSORTIUM THAT BECAUSE OF SERIOUS FOREIGN EXCHANGE POSITION A MORATORIUM APPLIES QUOTE ON CONVERSIONS FOR A PERIOD OF SIX MONTHS IN RESPECT TO MATURITIES OF PRINCIPAL AND INTEREST FALLING DUE FROM ONE MAY 1971 ON ALL CREDITS OBTAINED UNDER CONSORTIUM AUSPICES ENDQUOTE AND THAT DURING MORATORIUM PAKISTAN WILL MAKE DEBT SERVICE PAYMENTS INTO CREDITOR GOVERNMENTS' RUPEE ACCOUNTS IN PAKISTAN STOP GOVERNMENT HAS EMPHASIZED ITS DETERMINATION TO MEET ALL CONTRACTUAL OBLIGATIONS AND POINTS TO RUPEE PAYMENTS TO BE MADE ON DUE DATES AS EVIDENCE OF GOOD FAITH STOP APPARENTLY ALL INDUS TARBELA LOANS EXEMPTED FROM MORATORIUM STOP IT IS NOT YET CLEAR WHETHER THESE MEASURES APPLY ALSO TO COMMERCIAL DEBT STOP THERE ARE INDICATIONS BUT TO DATE INCOMPLETE EVIDENCE THAT SIMILAR ACTION BEING TAKEN WITH NON-CONSORTIUM COUNTRIES STOP BANK/IDA HAS NOT REPEAT NOT BEEN NOTIFIED THAT MORATORIUM WILL APPLY FOR PAYMENTS DUE TO BANK GROUP PARA

IN ORDER ALLOW EXCHANGE OF VIEWS ON SITUATION CARGILL CHAIRED INFORMAL CONSORTIUM MEETING APRIL 30 IN PARIS AT WHICH FARRELLY REPRESENTED ASIANBANK STOP SUBSEQUENTLY CARGILL VISITED ISLAMABAD FOR MEETINGS WITH PRESIDENT AND OFFICIALS STOP FIRST INCOMPLETE REPORTS FROM THOSE MEETINGS INDICATE PAKISTAN'S FINANCIAL SITUATION EXTREMELY SERIOUS WITH VERY HIGH BUDGET DEFICIT STOP FOREIGN EXCHANGE RESERVE POSITION ALREADY TIGHT AND COULD BECOME CRITICAL BY JULY IN ABSENCE OF REMEDIAL MEASURES WHICH AS FAR AS WE KNOW GOVERNMENT HAS NOT YET FORMULATED PARA

SHORTLY BEFORE PARIS MEETING PAKISTAN HAD REQUESTED STANDBY ASSISTANCE FROM FUND BASED ON REFORM PACKAGE PREPARED EARLIER THIS YEAR STOP SITUATION NOW SUBSTANTIALLY DIFFERENT AND EYE BELIEVE FUND COMMA PRIOR TO ANY STANDBY ASSISTANCE COMMA WILL REQUIRE REALISTIC ECONOMIC PROGRAM FROM GOVERNMENT AND REVIEW BY FUND MISSION PARA

CARGILL RETURNING WASHINGTON TOMORROW STOP ECONOMIC ADVISOR TO PAKISTAN PRESIDENT ALSO ARRIVING OVER WEEKEND FOR CONSULTATIONS STOP EYE WILL COMMUNICATE WITH YOU AGAIN NEXT WEEK WHEN FURTHER INFORMATION ON GENERAL SITUATION AVAILABLE PARA

DECLASSIFIED
SEP 25 2012
WBG ARCHIVES

REGARDING OPERATIONS BANK/IDA PRESENTLY NOT PROPOSING ANY NEW LOANS OR CREDITS BUT CONTINUING DISBURSEMENTS TO SUPPLIERS AND BANKS UNDER EXISTING LOANS AND CREDITS STOP SIMILAR POSITION INDICATED BY ALL CONSORTIUM COUNTRIES AT PARIS MEETING STOP REGARDS SINCERELY

MC NAMARA"

Mr. Watanabe is President of the Asian Development Bank in Manila.

Thank you very much for your assistance.

489/B/2

HARVARD UNIVERSITY

DEVELOPMENT ADVISORY SERVICE

OF THE

CENTER FOR INTERNATIONAL AFFAIRS

1737 Cambridge Street
Cambridge, Massachusetts 02138

(617) 495-2165 & 495-2164
Cable Address: DASHARVARD

April 6, 1971

IBRD IDA
WBG
ARCHIVES

President Robert S. McNamara
World Bank
1818 H Street, N.W.
Washington, D. C. 20433

Dear Bob:

I am enclosing a memo that a couple of my colleagues and I prepared on the situation in East Pakistan. We have sent it to a few Senators and Congressmen, but are not making it public.

I am going to be in Washington next week and would like to see you on a couple of matters if you are going to be there. I'll get in touch with your secretary.

Sincerely yours,

ES

Edward S. Mason

Enclosure
ESM:w

President has seen

489 B/2

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ES

Edward S. Mason

Enclosure
ESM:w

COMMUNICATIONS
SECTION

1971 APR -8 AM 8:21

President has seen

RECEIVED

H.4200

CONFLICT IN EAST PAKISTAN: BACKGROUND AND PROSPECTS

Edward S. Mason
Robert Dorfman
Stephen A. Marglin

April 1, 1971

About the authors. . .

Edward S. Mason is Lamont University Professor Emeritus at Harvard University, and a former Dean of the Graduate School of Public Administration. He is a past-President of the American Economic Association, and a long-time advisor to the United States Government and the World Bank. In 1954/55 he directed an eight-man team that drew up the first development plan for Pakistan, and has had a long and continuing involvement with the problems of the development of Pakistan and other countries. Mr. Mason was most recently a member of the Petersen Commission on foreign aid appointed by President Nixon.

Robert Dorfman is professor of economics at Harvard University. He has been concerned with the problems of Pakistan development since 1961, when he became a member of the White House-Interior Team appointed by President Kennedy at the request of the then-President of Pakistan, Ayub Khan, to advise the Government of Pakistan on problems of water-logging and salinity. Mr. Dorfman has recently been a consultant to the World Bank on the development of the Lower Mekong River Basin.

Stephen A. Marglin is professor of economics at Harvard University. He has advised governments in Asia, Africa, and Latin America on problems of economic development, as well as the United States Government, the World Bank, and the United Nations.

CONFLICT IN EAST PAKISTAN: BACKGROUND AND PROSPECTS

I

Summary

The independence of East Pakistan is inevitable. What started as a movement for economic autonomy within the framework of a united Pakistan has been irrevocably transformed by the wholesale slaughter of East Pakistani civilians into a movement that sooner or later will produce an independent East Pakistan--"Bangla Desh" is a matter of time. A complete discussion of the Pakistani question would include an analysis of cultural, linguistic, and social issues, which along with economics and politics, are at the heart of the present conflict. This paper has a more limited goal: to assess the economic and political bases of disaffection in East Pakistan and to suggest the likely implications for international relations of the break-up of Pakistan.

In brief, the fact of a large and widening gap in the average standard of living between the two regions of the country is incontestable. Even the West Pakistani-dominated Government admits that the average East Pakistani must make do with barely two-thirds the average income in the West, and he faces higher prices too. The East Pakistanis argue that income disparity is largely the result of a systematic subordination of the interests of the Eastern region to those of the West; specifically, the East Pakistinis charge that allocation of foreign exchange--both that earned by the export of East Pakistani jute and that provided by foreign aid--disproportionately favors West Pakistan; that allocation of domestic investment reinforces the income disparity; and that high tariffs and import quotas raise prices to East Pakistanis in order to provide profits and jobs in West Pakistan.

We believe that in the main the facts support these charges. Pakistan Government policies have at the very least exacerbated the inequalities that arise from an uneven distribution of natural resources between the two regions, and a disproportionate share of the benefits of economic devleopment have accrued to West Pakistan.

The political program of Sheikh Mujib's Awami League, overwhelmingly endorsed by the people of East Pakistan in the recent elections, sought to correct these disparities by transferring control over economic policy from the Central Government to the provinces. The response of the Yahya Khan's Government has been to unleash a reign of terror whose full dimensions are only gradually becoming known.

The West Pakistani Army can delay independence, but terrain and logistics, coupled with the implacable hostility of the East Pakistanis to what has become foreign domination, are on the side of "Bangla Desh". Apart from the elementary and overwhelming humanitarian interest in an end to further bloodshed, American interest lies with a quick rather than a slow realization of independence. Most important,

tensions in South Asia will be reduced. Bangla Desh and India will develop mutually advantageous economic and cultural relations, a move long desired by both sides but frustrated by West Pakistanis who have refused to countenance any normalization of relations in the East as long as the Kashmir issue remains outstanding. The Kashmir issue too is likely to subside in importance, not because of any reduction in tension in the West--the Kashmir issue has never aroused much interest in the East--but because West Pakistan, without the economic support of the East, will be unable to sustain the level of pressure it has been able to mount until now. In short, Bangla Desh will be a truly independent state, ready and able to maintain normal relations with its neighbors and the powerful nations of both blocs, but a satellite or pawn of no one.

The independence of Bangla Desh will be inimical to American interests only insofar as American aid is used to delay the inevitable. Economic aid to the Pakistan Government should be immediately suspended. The "one-time" exception made last year to the embargo of arms sales and military aid (imposed after the Indo-Pakistani war of 1965) should be rescinded. American arms must not be supplied to a government that makes war on helpless civilians.

II

U.S. Economic and Military Aid to Pakistan

Since 1951 Pakistan has been a major recipient of U.S. economic aid amounting to approximately $3 billion[1] by 1969. Except for food aid donated under Public Law 480, the bulk of this assistance has been used to support industrialization in West Pakistan, with only a handful of projects undertaken in East Pakistan.

The quantum of U.S. military aid to Pakistan is a classified figure but two estimates[2] put it between $1.5 to $2 billion for the period between 1954 and 1965. The assistance has included F-104 Starfighters, Patton tanks, armoured personnel carriers, automatic and recoilless infantry weapons. This impressive array of modern weaponry was given expressly[3] for defensive purposes. With Pakistan an early member of SEATO and CENTO this military aid was intended to bolster the armed containment of the Communist Bloc in the Dulles era of U.S. foreign policy but apart from the brief border war with India of 1965 the only active use of these sophisticated weapons has occured against the unarmed and defenseless civilian population of EAst Pakistan.[4]

The growth and maintenance of the superstructure of the armed forces which was built up with massive U.S. military aid continued even after 1965 when the United States decided to put an embargo on the delivery of arms to both Pakistan and India. This was made possible by diverting resources from the much needed development projects. East Pakistan, poorer and less powerful politically than the West, suffered more by this irrational policy.

Surprisingly, the United States has just recently (October 1970) made an exception to its embargo on military sales to Pakistan. According to the information available, the United States has offered to supply Paksitan the following items:

(a) Armored personnel carriers (approximately 300)
(b) Maritime reconnaissance aircraft (4)
(c) F-104 jet fighters (6)
(d) B-57 bombers (7)

Fortunately, no sales or deliveries have yet been made. It is not too late to rescind the offer, a move that would be of practical as well as symbolic value.

III

Economic and Political Domination of East ~~and~~ by West

The basic facts seem to support the East Pakistan charge of economic domination by the West. The economic disparities between East and West Pakistan have been so serious for so long that the Pakistan government's highest planning authority has been forced to take official note of them.

A recent report[5] by a panel of experts to The Planning Commission of the Government of Pakistan provides authoritative documentation of the widening of economic disparities in the two regions. The most striking fact in this report is the widening gap between the income of the average West Pakistani and his Eastern counterpart. In 1959-60, the per capita income in West Pakistan was 32% higher than in the East. Over the next ten years the annual rate of growth of income of West Pakistan was 6.2% while it was only 4.2% in East Pakistan. As a result, by 1969-70 the per capita income of the West was 61% higher than in the East.[6] Thus in ten years the income gap doubled in percentage terms; it increased even more in absolute terms.

East Pakistanis blame three instruments of central government policy for their plight:

1. Pakistan's scant investible resources, plus foreign aid, are directed unduly to the development of West Pakistan--to the comparative neglect of East Pakistan.

2. In particular, East Pakistan's foreign trade earnings are diverted to finance imports for West Pakistan.

3. Economic policy favors West Pakistan at the expense of the East. Specifically, tariffs, import controls, and industrial licensing compel East Pakistan to purchase commodities from West Pakistan which, but for the controls, they could obtain more cheaply in world markets.

We believe the East Pakistani claims to be largely justified. First, it is indisputable that the bulk of public investment has been in West Pakistan though the majority of the population lies in the East. With 60% of the population, East Pakistan's share of central government development expenditure has been as low as 20% during 1950/51-1954/55, attaining a peak of 36% during the Third Five Year Plan period 1965/66-1969/70. East Pakistan has received an even smaller share of private investment, less than 25%.[7]

It may be true, as defenders of Pakistan government policy claim, that the great bulk of worthwhile investment opportunities have been in the West, though the relative attractiveness of the West may be more the effect of overall government policy than a cause. In any event the fact remains that investments in the West have done little or nothing for the people in the East.

As for the second point, it is clear that foreign exchange has been allocated to the detriment of East Pakistan. Over the last two decades East Pakistan's share of total Pakistan export earnings has varied between 50% and 70%, while its share of imports has been in the range of 25% to 30%.[8] Until 1962/63 East Pakistan has shown significant surpluses on foreign account, which has changed in recent years to small deficits. By contrast the West's foreign trade has shown a substantial and chronic deficit that has absorbed virtually all foreign exchange made available through foreign aid.

With respect to the third point, general economic policy has clearly favored West Pakistan. The West's preponderant share of imports and investments might have provided inexpensive necessities for all of Pakistan's people. In fact it has allowed the development of inefficient[9] industries, which, ironically, have prospered largely because of tariffs and quotas that have made East Pakistan a captive market. 40% of all exports of West Pakistan are sold to East Pakistan; in 1968/69 the West sold 50% more to the East than it bought from the East.

An analysis of foreign trade data reveals that a net transfer of resources has taken place from East to West Pakistan. According to the official report referred to above, East Pakistan has transferred approximately $2.6 billion to West Pakistan over the period 1948-49 to 1968-69.[10]

In short, Pakistan's economic policies are harmful to East Pakistan. "Exploitation" may be a strong word, but it seems clear, all in all, that East Pakistan's economic interests have been subordinated to those of the West, and that the East Pakistanis have had good cause to resent that fact.

The economic domination of East Pakistan has been facilitated by West Pakistani dominance of the Central Government. The military regime in Pakistan has existed, with modifications, since 1958, and decision-making authority rests with a well-entrenched civil service and their military bosses. <u>All</u> senior military members of the administration have been West Pakistani, and of the senior officers in the Central civil services, 87% were West Pakistani in 1960,[11] and the proportion has not changed much since. The Deputy Chairman of the Planning Commission and the Central Finance Minister, key individuals in resource allocation, have always been West Pakistanis.

The location of the Central Government in West Pakistan has encouraged the concentration of industry and the entrepreneurial class in West Pakistan.[12] Such a concentration is to be expected in an economic system where direct allocational control of resources by the government makes direct access to government authorities a prime business asset.

IV

Background to the Break-Up of Pakistan

The history of economic and political domination of East Pakistan by the West led naturally to increasing demands for provincial autonomy, spearheaded by Sheikh Mujibur Rahman's Awami League. Its 6-point platform for autonomy sought to transfer control over foreign trade, foreign aid allocation, and taxation powers to the provinces so that no province could be dominated through disproportionate control of the Central Government's powers over resource allocation.[13]

At the polls last December this Awami League platform swept 167 of the 169 seats in the National Constitutional Assembly that were alloted to East Pakistan. The Awami League's 167 seats constituted an absolute majority in a chamber of 313. The political and military powers of West Pakistan tried to pressure Sheikh Mujib into compromising on his 6-point autonomy mandate. In particular Zulfikar Ali Bhutto, leader of the West Pakistani People's Party which had won 80-odd seats in the elections, demanded that control of trade and aid should remain with the Central Government. When Sheikh Mujib refused to compromise on these instruments of past economic domination, Bhutto announced a boycott of the Constitutional Assembly scheduled to meet on March 3. General Yayha Khan used this pretext to postpone the Assembly indefinitely. This arbitary postponement provoked deomonstrations in Dacca and other cities on March 1, which the military decided to control by force. The military authorities conceded 172 deaths in the disturbances (the Dacca correspondent ot the London Observer put the figure nearer 2000). Despite this bloody provocation the Awami League refrained from declaring independence. Instead they launched a campaign of civil disobedience to demand a return of troops to barracks and an enquiry into the firings. The campaign of non-cooperation effectively transferred civilian authority to Sheikh Mujib but even in the massive rally of March 7 Sheikh Mujib still spoke of a united Pakistan with autonomy for each province. His preparedness for negotiation and commitment to the unity of Pakistan was demonstrated by his continuation of talks for the next two weeks despite the well-advertised influx of West Pakistani troops. Indeed, in retrospect it would appear that the West Pakistani officials were never negotiating in good faith; negotiations were a way to forestall an open break until sufficient numbers of West Pakistani troops could be brought on the scene to unleash a terror whose full dimensions are only now becoming known. The Awami League's commitment to a peaceful political settlement was convincingly demonstrated by the complete lack of preparation of the civilian population to the onslaught[14] of military arms which was unleashed on them on the night of Thursday March 25.

V

International Implications of an Independent "Bangla Desh"

From news reports now available it would appear that the use of massive military fire power has broken the Awami League and its supporters in most urban centers. But control of urban centers at gunpoint in a country where 90% of the population lives in rural areas hardly constitutes a framework for any effective government, let alone a popular one. The immediate prospect is for ruthless military rule in urban centers, with tenuous control over a countryside which is likely to become increasingly the base for armed guerilla resistance.

The base for such a movement clearly exists. The overwhelming support for the Awami League's demand for autonomy was clearly shown in the election results of December when 167 out of 169 seats allotted to East Pakistan were won by the League.[15] As reports of military massacres are carried by urban refugees to the rural areas, the democratically expressed sentiment for autonomy is likely to be converted to a militant desire for independence. It is possible that a West Pakistani army of occupation can suppress the Bengali nation for two months, six months, or a year, but the American experience in Vietnam illustrates only too painfully the impossibility of holding an entire population captive by force of alien arms alone.

The emergence of an independent Bangla Desh appears to be inevitable in the long run. What remains in question is how much blood will flow before it occurs. Politically it is clear that the longer it takes to achieve independence, the more likely it is that control of the independence movement will slip away from the moderate leadership of the Awami League to the more leftist National Awami Party (which did not contest the December elections).

Assuming that the independence movement succeeds while under Awami League control, certain predictions may be made about its relations with neighbors and super-powers. As expressed in public statements of Sheikh Mujib, an independent Bangla Desh will establish friendly relations with India and set up economic trade to their mutual advantage. Up to now such trade--and all cultural ties--have been frustrated by the West Pakistanis who dominate the Central Government. They believe that, short of war, their only lever to force a settlement of their Kashmir claim is the economic interest of India in trade with East Pakistan. By contrast, East Pakistan has never been aroused by Kashmir, and in the 1965 war no military activity took place within its borders. Strong linguistic and cultural ties with the state of West Bengal in India are likely to help cement durable good relations between the two countries and reduce tension in the area. Unable to share the burden of military expenditures with teh East, West Pakistan is bound to tone down its policy of controntation with India, a confrontation which for the past 24 years has diverted scarce resources of both these poor, populous countries from much needed economic development to defense.

As an independent nation Bangla Desh might conceivably establish marginal economic contacts with Communist China. But these are unlikely to be any greater than the current scale of trade and aid between China and Pakistan, and will certainly be less than the likely range and depth of East Bengal's economic ties to neighboring India. As long as India is the main trading partner (and both pronouncements of Awami League leaders and the economic geography of the region support this possibility), it is unlikely that Bangla Desh will become a satellite of Communist China.

The U.S.S.R. has in the past three years become an active patron of the military clique that controls Pakistan. Soviet aid has included considerable economic aid (including agreements for a steel mill in West Pakistan) and some military aid. The Soviet initiative has been largely a response to growing Communist Chinese ties with Pakistan. This competition between rival giants has redounded to the benefit of West Pakistan where the central government and military establishment are based. The U.S.S.R. has not been sensitive to the aspirations of East Pakistanis in the past, and is unlikely to make a new Bangla Desh an arena for superpower competition for influence.

A major goal of U.S. foreign policy in this area has been the reduciton of the debilitating confrontation between India and Pakistan. This goal will surely be advanced by the existence of an independent Bangla Desh friendly to India. Most observers believe that the Awami League leadership will follow a neutral foreign policy, particularly if the U.S. and multilateral aid agencies like the World Bank are the major aid donors.

Bengali independence will be inimical to American interests only if by following short-sighted policies we drive East Pakistan into the arms of another power--the U.S.S.R. or China. To the extent that Bengali independence is delayed by means of American arms, the image of the United States will suffer, and rightly so. The offer of arms to Pakistan by the United States Government in October 1970, whatever its ostensible purpose, will, if implemented, oil a Pakistani military machine that is making war on its own citizens. The United States Government must rescind this offer forthwith. No further military aid, or economic aid--which directly or indirectly provides foreign exchange that makes it possible to buy weapons abroad--should be given to West Pakistan until it withdraws its occupation force from East Bengal and recognizes the independence of the Bengali nation.

Notes

1. Stern, J. J. and Falcon, W. P., Growth and Development in Pakistan 1955-69, Occaional Paper No. 23, Harvard Center for International Affairs, April 1970; M. A. Sattar, United States Aid and Pakistan's Economic Development, unpublished Ph.D. dissertation, Tufts University, 1969.

2. New York Times, September 28, 1964; Frank N. Trager, "United States and Pakistan," Orbis Vol. IX, Fall 1965, No. 3.

3. Formal agreement signed May 1954, reported in Department of State Press release, Department of State Bulletin, May 31, 1954, pp. 850-851.

4. Washington Post, March 30; New York Times, March 29 and March 30. These contain eyewitness accounts by correspondents of use of U.S. supplied tanks.

5. Reports of the Advisory Panels for the Fourth Five Year Plan 1970-75, Vol. I; Planning Commission, Government of Pakistan, July, 1970.

6. Ibid., p. 2, Table 1. As the report notes these estimates of disparity are understatements because of a lack of adjustment in the basic official data for the generally higher prices which prevail in East compared to West.

7. Ibid., p. 6, table 2.

8. Total foreign exchange available for imports is made up of export earnings and foreign aid. All data on trade are compiled from official statistics issued by the Central Statistical Office, Government of Pakistan.

9. Lewis, Stephen R., Pakistan: Industrialization and Trade Policies, O.E.C.D., Oxford University Press, 1970.

10. Planning Commission, op. cit., appendix 3.

11. Rahman, A., East and West Pakistan: A Problem in Political Economy of Regional Planning, Occasional Paper No. 20, Harvard University Center for International Affairs, 1968. By 1966, among all Class I officers in the Central Government East Pakistan's share was only 20 per cent.

12. Papanek, G. F., Pakistan's Development: Social Goals and Private Inventives, Harvard University Press, 1967.

13. The Six Points are:

(1) Establishment of a federation "on the basis of the Lahore Resolution and the Parliamentary framework of government with supremacy of legislature directly elected on the basis of adult franchise."

(2) Federal government shall deal with only two subjects, that is, defense and foreign affairs, and all other residuary subjects should rest in the federating states.

(3) There should be either two separate but freely convertible currencies for the two wings or one currency for the whole country provided that effective constitutional provisions were made to stop the flight of capital from East to West Pakistan. There should be separate banking reserves and a separate fiscal and monetary policy for East Pakistan.

(4) Denial to the Central Government of the right of taxation; vesting of tax provisions in the hands of the federating states with the Central Government receiving a fixed share.

(5) Foreign trade; Five steps shall be taken:
- (a) There shall be two separate accounts for foreign exchange earnings.
- (b) Earnings of East Pakistan shall be under the control of East Pakistan and the same for West Pakistan.
- (c) Foreign exchange requirements of the federal government shall be met by the two wings either equally or in a ratio to be fixed.
- (d) Indigenous products shall move free of duty within the two wings.
- (e) The constitution shall empower the unit governments to establish trade and commercial relations with, set up trade missions in and enter into agreements with foreign countries.

(6) Set up a militia or para military force by East Pakistan.

14. Preplanned according to reports by foreign correspondents, e.g. Sydney Schanberg in New York Times, March 26-29.

15. The eyewitness account of a British correspondent in Washington Post March 30 leaves no doubt about the appropriateness of the word "massacre".

489/3/1

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT
WASHINGTON, D.C. 20433, U.S.A.

OFFICE OF THE PRESIDENT

3/17/71
[via Bob W]

To Secretary Connally

Dear John

The International Development Association is facing "bankruptcy" July 1. I have outlined the problem in the attached memorandum and have suggested a course of action.

May we discuss the matter after you have had time to consider it.

With best wishes

Bob

3/30/71
John agreed I can say the US govt,
1. Believes the IDA bill will not pass the Congress by 7/1/71 and believes the legislation will pass the Congress by 12/31/71,
2. Supports action by the Pres of the Bk to obtain voluntary contributions to IDA's replenishment to permit operations after 7/1/71
3. In the person of the Pres, strongly supports the 3rd Replen.

NOTE ON ACTION REQUIRED TO REPLENISH THE COMMITMENT AUTHORITY OF THE INTERNATIONAL DEVELOPMENT ASSOCIATION

The International Development Association (IDA) will have exhausted its existing authority to make new loans by June 30, 1971. Unless action is taken immediately to replenish that authority, no new loans to such countries as India, Pakistan, and Indonesia may be made by the World Bank Group after that date. This note describes the nature of the problem and suggests a course of action to resolve it.

The IDA is an affiliate of the World Bank set up in 1960 to extend credits on very soft terms (10 years grace period; repayment over the following 40 years; with a service charge of 3/4 of 1%) to those countries which are too poor, or whose balance of payments is too weak, to enable them to accept loans on harder terms. Since IDA itself lends on soft terms, it cannot afford to borrow on the market and is therefore dependent for its funds on contributions from governments.

IDA's initial capital consisted of subscriptions of $1 billion, of which $765 million was subscribed by the governments of the developed countries (the so-called Part I member countries). Further replenishments took place in 1964 and 1969, amounting to $750 million and $1200 million respectively. In July, 1970, negotiations for a Third Replenishment in the amount of slightly over $2400 million over a three-year period (roughly $800 million a year, of which the U.S. was to contribute 40% or $320 million) were concluded between governments, and the Agreement is now awaiting action by legislatures. Under the terms of the Agreement, it cannot come into force until a notification has been received from member countries, including 12 Part I members, accounting for $1900 million of the contributions. This means that the arrangements cannot become effective without the notification of the United States Government.

It was made clear in the negotiations that by June 30, 1971, IDA would have fully committed the funds at its disposal and would therefore need fresh commitment authority (the necessary cash to finance disbursements, on the other hand, would be needed only over a period of approximately 7 years from the date of commitment). The negotiations were begun in the last few months of 1969 with the object of concluding them not later than July 31, 1970, thus allowing slightly less than a year for the necessary legislative action if the arrangements were to become effective by July 1, 1971. Ratification of the agreement by the U. S. Congress before July 1, 1971 now appears highly unlikely.

IDA already has in the pipeline projects amounting to $1.5 billion and, allowing for projects which may be discarded or delayed, planned commitments for the fiscal year beginning July 1, 1971 amount to $950 million. If there were to be a delay of no more than 6 months in Congressional ratification of the Third Replenishment (i.e., if Congress were to act by December 31, 1971), IDA would need to find about $450 million to cover commitments in the period July 1 to December 31, 1971. This might be done by asking member governments, other than the United States, to make voluntary contributions without waiting for the Agreement to become effective on the understanding that such contributions would count toward the discharge of their obligations once the arrangements came into force.

It is of the utmost importance for the work of IDA that there should be no delay in providing it with fresh commitment authority before July 1, 1971. The World Bank management needs to know, therefore:

1. What prospect the U.S. Administration sees that Congress will ratify the agreement by that date.

2. If Congressional ratification of the agreement cannot be achieved by July 1, what course of action the U.S. Government would recommend that the Bank management should follow.

If the U.S. Government were itself to conclude that the Congressional action required cannot be completed by July 1, IDA could ask for voluntary advance contributions from other member governments. In these circumstances, it would be of the greatest assistance if the U.S. Government would send a communication to the other Part I member governments saying (a) that it is the firm intention of the U.S. Administration to use all means at its disposal to secure the necessary action by the Congress as soon as possible after July 1, 1971, and that it has good hopes that such action can be completed not later than December 31, 1971, and (b) that, in the meantime, the U.S. Government would regard it as in every way helpful if other member governments would agree to make advance contributions since such action by them would help IDA to continue its operations without interruption.

3/13/71