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Foreign Asst.

/

1976 Budget
Session With The
President
12/10/74

1976 Budget
Session With The
President
12/10/74

GERALD R. FORD LIBRARY

MEETING WITH

ROY L. ASH

Tuesday, December 10, 1974

2

THE WHITE HOUSE

WASHINGTON

December 9, 1974

MEETING WITH ROY L. ASH
Tuesday, December 10, 1974
1:00 p.m. (60 minutes)
Oval Office

From: ~~Roy L. Ash~~

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I. PURPOSE

To review the issues raised by the FY 76 budget for International Programs and Selective Service.

II. BACKGROUND, PARTICIPANTS AND PRESS PLAN

A. Background: FY 76 budget submissions for International Programs and the Selective Service have been considered by OMB and members of the White House staff and the results of these reviews have been communicated to the affected agencies (with the single exception of the Export-Import Bank). This meeting will focus on the issues raised during the review process that require Presidential consideration and determinations.

B. Participants: Roy L. Ash, Paul O'Neill, Don Ogilvie, and Dale McOmber

C. Press Plan: David Kennerly photo.

III. TALKING POINTS

Don Ogilvie, would you describe the first issue we should consider in the international programs area?

THE WHITE HOUSE

WASHINGTON

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MEMORANDUM FOR: THE PRESIDENT

FROM: ROY L. ASH

SUBJECT: 1976 Budget decisions: Foreign Assistance

The agency requests and my recommendations with respect to 1976 budget amounts for Foreign Assistance are presented in the tabulations attached (Tab A).

Several key issues have been identified for your consideration (detail at Tab B).

1. AID development assistance.

State and AID recommend a total program of $1,194 million for development loans and grants, effectively about the same level as in the 1975 Budget, but an increase over 1974 and the likely appropriations for 1975. Our recommendation of $1,101 million reflects largely (a) deletion of loans to Indonesia ($20 million) because of that country's rapidly growing earnings from oil and to Morocco ($5 million) because of that country's earnings from phosphate exports; and (b) a decrease of $42 million in the $279 million requested for Latin America; our recommendation for Latin America is about the same as the 1974 level and probably higher than the amount Congress is likely to provide for 1975. The agency request for Indonesia, Morocco, and Latin America is based primarily on considerations of relationships with those countries.

The NSC agrees with our recommendation to delete loans to Indonesia and Morocco, but supports the State/AID recommendation on Latin America.

In addition, our recommendation provides a smaller increase in population programs, $23 million (compared to the requested increase of $37 million), for a total program of $161 million, or an increase of 43% over 1974 and 21% over the 1975 Budget. Also, our recommendation of $10 million for grants to American schools and hospitals abroad, AID's lowest priority program, is the level in the Budget in the last few years; AID wishes to anticipate the usual congressional add-on and proposes $22 million.

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E.O. 12356, Sec. 3.4 (b)
White House Guide Lines, Feb. 24, 1983
By DAD NARS, Date 6/27/85

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4

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Decision: Approve agency recommendation ______
Approve OMB recommendation ______

Other:

	Agency rec.	OMB rec.
Indonesia and Morocco	______	______
Latin America	______	______
Population program	______	______
American schools and hospitals	______	______

2. Inter-American Development Bank.

The next replenishment of the Bank's capital, now being negotiated, involves a $1,200 million U.S. share in three $400 million annual installments beginning in 1976. At issue is whether $240 million ($80 million annually) of the U.S. contribution should be paid-in capital, requiring budget outlays, or the entire U.S. contribution should be callable capital used as a guarantee for borrowing by the Bank, which does not result in outlays.

Treasury proposes paid-in capital to stimulate Latin American contributions, which do not, however, increase total resources flowing to the region, and to permit U.S. participation in a new non-regional fund with Japanese and European contributions. The NSC supports the Treasury proposal. Neither of these benefits justify, in our view, paid-in capital and resulting outlays.

Decision: Approve agency recommendation ______
Approve OMB recommendation ______

3. Vietnam economic aid.

State and AID recommend $725 million, slightly lower than the 1975 Budget request of $750. The request is much higher than Congress will provide this year and represents substantial "cut insurance." The NSC supports the request. The OMB recommendation of $550 million is close to the minimum import financing need of Vietnam estimated at about $500 million, below which the economy would suffer a severe setback. A middle option is $650 million, which would provide some cut insurance and would probably be more defensible before Congress than the State/AID request. All options provide the necessary amounts to maintain current consumption levels in Vietnam.

Decision: Approve agency recommendation ______
Approve OMB recommendation ______
Approve middle option ______

4. Cambodia economic aid.

State and AID recommend $156 million, which, in addition to maintaining the level of imports into Cambodia, adds amounts for petroleum and fertilizer. The NSC supports the State/AID request. The OMB recommendation of $132 million deletes the additional amounts on the grounds that demand for petroleum has declined and food production depends on the military situation more than on more fertilizer.

Decision: Approve agency recommendation ______
Approve OMB recommendation ______

5. Cambodia military aid.

State recommends $450 million, compared to about $400 million in 1974 and 1975. The NSC supports the State request. Defense recommends $400 million. OMB believes Defense's judgment is superior on Cambodia's requirements for ammunition and other military consumables.

Decision: Approve State and NSC recommendation ______
Approve DOD and OMB recommendation ______

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6. Middle East economic and military aid.

The total 1975 Budget request for the special Middle East package was $908 million for Israel, Egypt, Jordan, and Syria. State's recommendation of $1,023 million for 1976 includes economic aid increases of $50 million for Egypt, $50 million for Israel, and $15 million for Syria. This recommendation is designed to signal continued confidence in the negotiating process and offer a bigger incentive for cooperation in a peaceful settlement. The NSC supports the State request.

The OMB recommendation of $775 million repeats the 1975 request, and thereby is neutral in its signals, with the exception of a reduction in economic and military aid to Jordan from $208 million to $75 million, reflecting the diminished role of Jordan as a result of the Rabat conference.

In economic terms, U.S. aid to Egypt, Jordan, and Syria is now relatively marginal, given the huge amounts of aid pledged by the Arab oil countries -- $7.6 billion in the year ending September 30.

Decision: Approve agency recommendation ______
Approve OMB recommendation ______

7. Phaseout of military aid grants.

Military grant aid (MAP), except for its training component, is under increasing criticism from Congress accompanied by attempts to terminate it or cut it severely with restrictions on its use. A new approach may be needed to preserve the grant program for situations where it is clearly necessary (e.g., active hostilities or other special circumstances) and to obtain an adequate military credit sales program to offset reductions in MAP.

State's recommendations for MAP, supported by NSC, phase out only one of 20 country programs in the period 1976-80 -- Korea by the end of 1977. The OMB recommendation is an explicit policy of phasing MAP programs by the end of 1977 (except for countries facing active hostilities or other special circumstances) and of increasing credit sales as an offset. Training programs would be retained in any phaseout. A third alternative, recommended by Defense, is initiate a shift to credit sales and to adopt an explicit phaseout of MAP over the period 1976-80, but not to single out, at this time, specific countries for phaseout after 1977.

In the context of this general policy question (Issue 7a at Tab B), five countries -- Turkey, Korea, Indonesia, Philippines, and Thailand -- and the small Latin American program ($11 million for 9 countries) are particular issues for 1976 and 1977 (Issues 7b-g at Tab B).

If you do not wish to make an explicit general policy decision now on phasing out MAP, OMB recommends that you direct that a study be conducted to develop alternative strategies for the military assistance and sales program through 1980, including, in particular, consideration of phaseout alternatives. The study should concentrate on developing recommendations that Congress could support and be completed in time for presentation to Congress in connection with its consideration of next year's Foreign Assistance Act.

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Decision:

No phaseout policy (State and NSC) ______
Phaseout by end 1977 (OMB) ______
Phaseout policy but no specific country decisions after 1977 (DOD) ______
A study of the issue ______

Apart from a decision on the general issue, your decision is needed on the particular programs for 1976 and 1977.

Turkey (Issue 7b)

State/NSC recommendation
($64 million in 1976; $46 million in 1977) ______

OMB recommendation
($50 million in 1976; $25 million and phaseout in 1977) ______

DOD recommendation
(Same amounts as OMB; no phaseout decision now) ______

Korea (Issue 7c)

State/NSC recommendation
($75 million in 1976; $50 million and phaseout in 1977) ______

OMB and DOD recommendation
($50 million in 1976; $25 million and phaseout in 1977) ______

Indonesia (Issue 7d)

State/NSC recommendation
($21 million in 1976; $19 million in 1977) ______

OMB recommendation
($5 million and phaseout in 1976) ______

DOD recommendation
(Same amounts as State; no phaseout decision now) ______

Philippines (Issue 7e)

State/NSC recommendation
($20 million in 1976 and 1977) ______

OMB recommendation
($10 million in 1976; $5 million and phaseout in 1977) ______

DOD recommendation
(Same amounts as State; no phaseout decision now) ______

Thailand (Issue 7f)

State/NSC recommendation
($30 million in 1976; $25 million in 1977) ______

OMB recommendation
($20 million in 1976; $10 million and phaseout in 1977) _____
DOD recommendation
($35 million in 1976 and 1977; no phaseout decision now) _____

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Latin America (Issue 7g)

State/NSC recommendation
($10 million in 1976; $8 million in 1977) _____
OMB and DOD recommendation
($4 million and phaseout in 1976) _____

8. Latin America military credit sales.

State recommends $202 million for 1976 and $246 million for 1977. The NSC supports the State request. The OMB recommends (Defense concurs) $200 million in each year, the same as that budgeted for 1975.

State wishes to continue credit sales to Venezuela and to increase them to Argentina and Brazil. The OMB recommendation deletes the program for Venezuela, which as an oil rich country is easily able to finance its own purchases. Brazil and Argentina are able increasingly to pay cash or find commercial credit for their U.S. arms purchase. All priority needs can be met within the overall $200 million level.

Decision: Approve State and NSC recommendation _____
Approve OMB and DOD recommendation _____

9. Morocco military credit sales.

State recommends $30 million for 1976, compared to $14 million in 1975, which was itself an increase over previous levels as a result of the good reception Secretary Kissinger was given there last year. The proposed increase for 1976 results from a subsequent visit and would help finance a force modernization program. The NSC supports the State request.

OMB recommends (Defense concurs) continuation of the $14 million level. Morocco, because of its windfall earnings from phosphate exports and its access to Arab oil money, can finance needed U.S. arms purchases.

Decision: Approve State and NSC recommendation _____
Approve OMB and DOD recommendation _____

10. Greece military credit sales.

State recommends $105 million for 1976 and $110 million for 1977, compared to $71 million in each of the prior two years. The NSC supports the State request. These increases are designed to help restore U.S. influence and indicate approval of the restoration of democracy. They would finance payment on Greece's large purchases last summer and a substantial amount of new purchases.

OMB recommends (Defense concurs) $90 million annually in 1976 and 1977. This level would also signal favorable U.S. attitudes, finance payments on recent purchases, and provide a modest amount for additional purchases. Although a significant increase over prior years, the OMB recommendation would be less likely to be perceived as contributing to a Greece-Turkey arms race.

Decision: Approve State and NSC recommendation ______
Approve OMB and DOD recommendation ______

In addition, your decision will be needed on P.L. 480 food aid for 1975 and 1976. Alternatives are now being prepared and will be available for our discussion of the foreign aid budget. It appears now that the alternatives for 1975 will exceed the original 1975 Budget outlays of $742 million by $200-600 million. The alternatives for 1976 will range from $861 million to $1,181 million.

Attachments

cc:
DO Records - Official file
Director
Director's chron
Deputy Director
Mr. Ogilvie
BRD
Mr. Frey

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IAD:JMFrey:neh:12/6/74

Tab A - Summary Data

FOREIGN ASSISTANCE 1974-76
Program, Budget Authority, Outlays
($ millions)

	PROGRAM (Obligations)				
		1975		1976	
	1974	Budget amended	Estimate	Agency Request	OMB Recommend.
SECURITY ASSISTANCE					
A. Supporting Assistance	132	498	698	620	453
B. Indochina Postwar Reconstruction	502	943	574	965	764
C. Military Assistance	4,724	3,497	2,202	2,916	2,697
Grant MAP	793	1,024	629	878	671
Foreign Military Credit Sales	713	873	873	1,038	1,026
Military Assistance, Vietnam	1,018	1,600	700	1,000	1,000
Emergency Assistance, Israel	2,200	--	--	--	--
D. Total Security Assistance	5,358	4,938	3,474	4,501	3,914
DEVELOPMENT ASSISTANCE					
A. Multilateral	2,383	1,185	1,165	1,136	1,136
Intl. Financial Institutions	2,237	1,006	1,006	946	946
Intl. Organizations and Programs	146	179	159	190	190
B. Bilateral	1,057	1,405	1,197	1,246	1,153
Development Loans and Grants	877	1,139	931	1,172	1,091
Other AID Programs	145	231	231	64	52
Other Bilateral	35	35	35	10	10
C. Total Development Assistance	3,440	2,590	2,362	2,381	2,289
MIGRATION AND REFUGEE ASSISTANCE	50	9	61	11	23
PRESIDENT'S CONTINGENCY FUND	12	30	20	30	30
P.L. 480	850	872	1,093	1,247	945
TOTAL FOREIGN ASSISTANCE PROGRAM	9,710	8,439	7,010	8,170	7,201
TOTAL BUDGET AUTHORITY	8,594	7,143	5,547	7,098	6,115
TOTAL OUTLAYS	4,081	4,904	5,474	6,466	5,855

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INTERNATIONAL DEVELOPMENT ASSISTANCE

1976 Budget

Summary Data

	(In millions) Budget authority	(In millions) Outlays	Employment, end-of-period Full-time Permanent	Employment, end-of-period Total
1974 actual.................	3171	1459	9131	9467
1975 January budget.........	2095	1640	9704	10175
as amended.............	2100	1641	XXXX	XXXX
current estimate	1852	1685	8904	9394
1976 planning ceiling.......	1469	1623	XXXX	XXXX
agency recommendation..	1957	1730	8727	9208
OMB recommendation.....	1864	1618	8704	9186
Transition period				
agency recommendation..	302	430	8727	9208
OMB recommendation.....	198	368	8704	9186
1977 OMB estimate..........	1958	1529	8704	9186

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INTERNATIONAL SECURITY ASSISTANCE

1976 Budget

Summary Data

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(In millions)

	Budget Authority	Outlays
1974 actual	4813	1940
1975 January budget	3382	2116
as amended	4255	2491
current estimate	2863	2775
1976 planning ceiling	3019	2669
agency recommendation	4028	3520
OMB recommendation	3445	3330
Transition period		
agency recommendation	715	698
OMB recommendation	623	676
1977 OMB estimate	3021	3233

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E.O. 12356, Sec. 3.4 (b)
White House Guide Lines, Feb. 24, 1983
By KBH NARS, Date 6/27/85

Tab 8 - Issues

1. AID Development
Assistance

Foreign Assistance

1976 Budget

Issue #1: AID Development Assistance

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Statement of Issue

What should be the level of AID development assistance requested in the 1976 Budget?

	1974	1975 Budget	1976 Alt. #1 Agency Req.	1976 Alt. #2 OMB Rec.
	($ millions)			
Country Loans and Grants				
Asia	248	387	335	315
Latin America	232	281	279	237
Africa	108	152	184	179
Special disaster relief	48	126	--	--
Other	345	358	396	370
Total	981	1,304	1,194	1,101
of which				
Population programs	112	138	175	161
American Schools and Hospitals	19	10	22	10

Background

Over half of AID funds are targeted on Indochina and the Middle East (see separate issues). The remainder of the program, although called "developmental," is for a variety of foreign policy and humanitarian as well as economic development purposes.

The AID request, setting aside special disaster relief in 1975, is generally proposed for the same countries and at about the same levels as in the 1975 Budget.

Alternatives

#1. A $1,194 million AID development program, about the same total level as in the 1975 Budget (Agency req.).

#2. A $1,101 million program, which would (a) eliminate the part of the Latin America request which was based solely on the desire to maintain the 1975 Budget level; (b) eliminate loans to Indonesia and Morocco because of their large and growing export earnings; (c) eliminate the part of the population program

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increase related to expanded administrative support of U.S. non-profit institutions and other lower-priority activities; and, (d) hold the low-priority program of grants to American schools and hospitals abroad at the 1975 Budget level (OMB rec.).

Analysis

Country programs. The bulk of the AID request for loans and grants to Asia is for India, Pakistan, and Bangladesh. There is some doubt as to the extent to which these countries will use the aid effectively, but the need is so great that the proposed assistance appears warranted. The AID request, however, also includes $20 million in loans to Indonesia which is acquiring huge and growing foreign exchange reserves from oil revenues. State and AID believe continuation of concessionary loans is necessary to avoid upsetting the Indonesians in view of the sharp drop in assistance from $74 million in 1974. Because, however, there is no economic justification for the loans, and the Indonesians have accepted without difficulty a large reduction in aid already, OMB proposes that U.S. aid be limited to the $4 million technical assistance program proposed by AID.

The AID request for Africa reflects continued support for the Sahelian drought region as well as the numerous poorer countries of sub-Saharan Africa. AID, however, proposes a $5 million loan to Morocco, which has a huge foreign exchange windfall (over $1 billion) from phosphate fertilizer exports and is receiving substantial aid from Arab oil producers. OMB recommends that aid to Morocco be limited to the $2 million technical assistance program proposed by AID.

NSC shares the OMB view that development loans to Indonesia ($20 million) and Morocco ($5 million) would be difficult to justify based on their increased foreign exchange earnings arising from oil and phosphates, respectively. Moreover, inclusion of these requests could risk congressional reaction damaging prospects for the foreign aid bill.

The AID program for Latin America is widely scattered among some twenty countries, most of which are comparatively well-off and able to find alternative sources of financing. AID originally requested $237 million for the region, which was based on a review of project proposals. This amount was subsequently raised by $42 million primarily in order to keep aid at about the same level as in the 1975 Budget. The NSC strongly supports the $42 million add-on to support Inter-American initiatives. Secretary Kissinger, with the President's approval, assured the Latin Americans that our aid levels would be maintained. The Latins always look to the Administration's request as the evidence of U.S. intentions. OMB recommends that this add-on not be approved principally because it is not needed. The OMB proposed level of $237 million is larger than the actual program for Latin America in 1974 and probably will be higher than Congress will provide this year.

AID is also proposing an increase in population control programs from $138 million in the 1975 Budget to $175 million. Although this is a high-priority program, AID has been providing support to U.S. non-profit institutions and to paramedical training programs abroad for an extended period. In many of these cases, OMB believes that the LDC governments and institutions should begin to assume more direct responsibility for selecting the most effective programs to meet their needs. This would permit U.S. aid to be concentrated on more innovative or catalytic activities. Accordingly, OMB recommends that the program be increased by $23 million, to $161 million in 1976 (still over half of the total worldwide effort to support family planning in the LDC's).

Finally, AID is proposing that the Administration increase the budget request from $10 million to $22 million for American schools and hospitals abroad (ASHA), among the lowest priority programs of AID. The request is not based on program needs, but is designed primarily to anticipate the usual congressional add-on. OMB believes that this is inadvisable in a period of fiscal stringency.

Agency Request. A $1,194 million AID development program.

OMB Recommendation. A $1,101 million program.

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2. Inter- American
Development Bank

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Foreign Assistance

1976 Budget

Issue #2: Inter-American Development Bank

Statement of Issue

Should the U.S. pledge to the fourth replenishment of the Inter-American Development Bank's (IDB's) ordinary capital resources include $240 million in paid-in capital ($80 million in 1976)?

	1974	1975 Budget	1975 Est.	1976 Alt.#1 Agency Req.	1976 Alt.#2 OMB Rec.
	($ millions)				
Inter-American Development Bank:					
Ordinary Capital:	193			400 ?	400
Paid-in	(25)	--	--	(80)	(-)
Callable	(168)	--	--	(320)	(400)

Background

The United States provides development assistance through the multilateral International Financial Institutions (IFI's)--the World Bank Group, and the Inter-American, Asian and African Development Banks. IFI members formally commit themselves to provide funds to the institutions by making multi-year pledges and then provide actual contributions in annual installments. Most 1976 IFI contributions are installments on past commitments.

The only new IFI pledge calling for an installment to be appropriated in 1976 is the proposed replenishment of IDB ordinary capital funds from which loans are made to wealthier Latin American countries at near market terms. The Treasury, which manages U.S. participation in the IFI's, proposes that the United States continue to provide "paid-in" capital, which results in budget outlays, as well as "callable" capital, which is merely a guarantee for IDB borrowing in world capital markets and does not result in budget outlays.

Alternatives

#1. A $1,200 million U.S. contribution to be provided in three $400 million annual installments, to the replenishment of the IDB's ordinary capital ($80 million paid-in, $320 million callable) (Treasury req.).

#2. A $1,200 million U.S. contribution, entirely in callable capital (OMB rec.).

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Analysis

Paid-in capital is required when a bank is first set up to provide working capital and reserves until the bank's own loans and investments can generate the necessary earnings. The IDB's earnings are now sufficient for these purposes and additional paid-in capital would merely enable it to lower its interest rate slightly. Because there is no need to subsidize interest for the relatively wealthy ordinary capital borrowers, the United States is generally attempting to raise ordinary capital rates to more nearly reflect true borrowing costs.

The case for continuing the paid-in contribution to the IDB rests on several special considerations.

(1) The United States has expressed a desire to maintain a special relationship with Latin America.

(2) Treasury would like to use at least part of the U.S. contribution to join a new "non-regional" fund being created for Japanese and European contributions, which would require paid-in capital but offers no clear benefit to the United States.

(3) A U.S. paid-in contribution is necessary to encourage a paid-in contribution by the Latins. (However, since they would be borrowing the same funds back again, there is little benefit from paid-in contributions by the recipients.)

The NSC believes that the inclusion of a paid-in capital contribution as part of the fourth replenishment for the Inter-American Development Bank will best serve to encourage contributions from other participants. Accordingly the NSC supports Treasury's recommendation for a paid-in capital contribution of $240 million ($80 million in 1976) within the agreed total levels of the replenishment. OMB does not believe that the $240 million cost is worth the benefits of showing special treatment for Latin America, of participating in the new fund, or securing paid-in contributions from the recipients.

Agency Request: Alternative #1 - Treasury believes that the advantages of contributing to the new ordinary capital fund are worth the budgetary cost.

OMB Recommendation: Alternative #2 - The potential advantages of a paid-in contribution are primarily tactical--since it will have a negligible effect on the level of external resources made available to the Bank by other donors. Elimination of the paid-in contribution would, however, effect a significant outlay saving for the United States, reducing the paid-in portion by $80 million for each of the next three years.

3. Vietnam-
Economic Aid

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Foreign Assistance

1976 Budget

Issue #4: Indochina Postwar Reconstruction (IPR): South Vietnam

Statement of Issue

What level of economic assistance should be requested for South Vietnam for 1976?

	1974	1975 Budget	1975 Est.	1976 Alt.#1 Agency Req.	1976 Alt.#2	1976 Alt.#3 OMB Rec.
	($ millions)					
Import financing	333	550	360	525	525	500
Investment projects	50	200	50	200	125	50
Total, IPR	383	750	410	725	650	550

Background

U.S. assistance has enabled South Vietnam to survive the economic impact of the war, by providing imports to offset production losses and meet the inflationary demand resulting from spending to support the war effort. In addition, spending by the United States in support of its operations provided a major source of foreign exchange earnings. The sharp curtailment of this spending, continued security problems, and declining assistance levels have combined with global inflation to put the economy into recession.

U.S. assistance must continue to provide minimum consumption and investment requirements. The issue turns mainly on the amount of investment funds the economy can productively use, but also partly on the question of including insurance against congressional cuts.

Alternatives

#1. $725 million (State req.).

#2. $650 million.

#3. $550 million (OMB rec.).

Analysis

The economy of South Vietnam continues to be dependent on U.S. financed imports for survival as well as growth. The economy requires about $500 million in externally financed raw materials and essential consumption goods. A reduction in imports below this level would further reduce domestic production, necessitate continued devaluations, intensify inflation, and could force politically disruptive policy changes.

On the other hand, increasing imports significantly above the $500 million level would yield less clear benefits. Some portion of any increase would undoubtedly go for less essential consumption goods, although the Vietnamese government would try to channel most additional funds into investment. Such an effort is not likely to be effective in moving toward self-sustaining growth, however, until the security situation and economic policies improve. Without these improvements, little additional private sector investment is likely to occur, and the productivity of any public sector investment will be limited. Once the preconditions for investment are established, however, domestic capital, foreign investors, and aid from international financial institutions and other countries is likely to become available to meet investment needs.

For these reasons, OMB doubts the effectiveness of a large U.S. investment increment in boosting Vietnam toward economic self-sufficiency. A RAND cooperation study recently carried out for AID similarly questions the advisability of large capital investment projects given their inherent vulnerability and the current economic uncertainties.

The NSC strongly believes that the U.S. objective should be to develop economic self-sufficiency in Vietnam in the shortest possible time. It argues not only that this is a realistic objective, capitalizing on progress to date and favorable trends, but also that it will serve U.S. interests best both by strengthening the peace in Southeast Asia and by allowing an earlier phase-out of major U.S. economic aid. Accordingly, the NSC supports the State/AID recommended level ($725 million) as that most likely to achieve that objective.

The other argument which is made for a high request is that it is necessary to request more than the requirement to assure that Congress will actually appropriate sufficient funds. The record of recent congressional action on Executive Branch requests for Indochina economic assistance, however, calls this argument somewhat into question:

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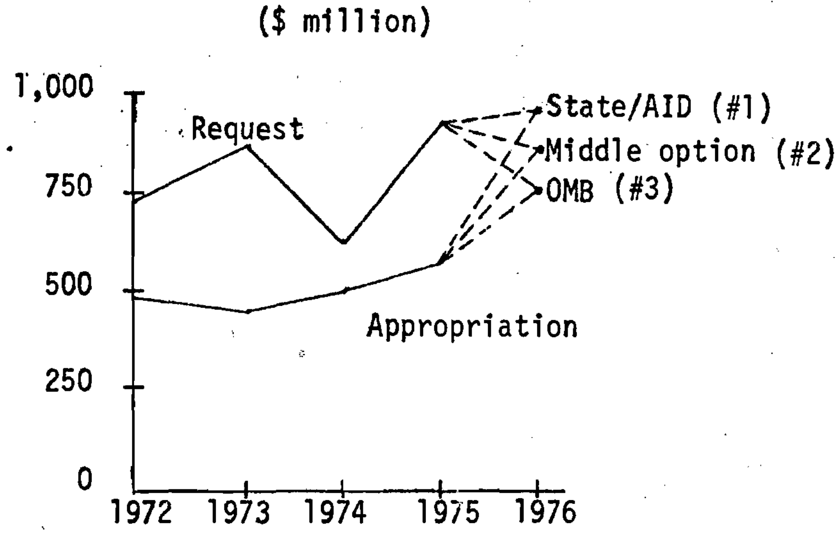

Secretary Kissinger responded to congressional pressures this July by providing a five-year phase-out plan for IPR assistance. This plan had the objective of achieving self-sustaining growth, and virtually ending assistance, by 1980. Congress is not responding favorably to this initiative, however, and it appears that there will continue to be little relation between the budget requests and actual appropriations.

Alternative #1, $725 million, would allow for perhaps $200 million in investment. This is too high to be justified persuasively, and would invite deep congressional cuts. Alternative #2, $650 million, is a middle course. It would allow $100-150 million for investment and/or insurance against possible cuts. Alternative #3, $550 million, is much closer to actual requirements, and could be strongly defended as a minimum program, but would rely primarily on changed conditions to call forth investment. This alternative would not provide much cut insurance.

Agency Request: Alternative #1 - $725 million.

OMB Recommendation: Alternative #3 - $550 million.

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4. Cambodia-Economic Aid

FOREIGN ASSISTANCE

1976 Budget

Issue# 5 : Military Assistance to Cambodia

Statement of Issue

How much grant military assistance is required in 1976-1977 to sustain the friendly Cambodian forces?

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	1974	1975		1976		1977
	Actual	Budget	Est.	Alt. #1 State Req.	Alt. #2 DOD/OMB Rec.	State/DOD/OMB Rec.
	($ millions)					
Grant MAP	412	390	400	450	400	350

425

Background

With minor exceptions in the Navy and Air Force, the GKR's forces were developed to the fullest extent with 1970-1974 funds and the 1975 effort has been limited almost exclusively to operations and maintenance costs with ammunition and POL as the major components, as will be the case in 1976. Efforts to expand and further modernize the GKR ground forces were terminated because of a combination of factors including skyrocketing prices and the realization that the Army at its current size and effectiveness is all that the Cambodian government can produce.

Alternatives

#1. Request $450 million for 1976 and project $350 million for 1977 (State req.).

#2. Request $400 million for 1976 and project $350 million for 1977 (DOD/OMB rec.).

Analysis

As Alternatives #1 and #2 for 1976 are designed to accomplish essentially the same ends and the lower level is supported by DOD, whose judgment should be superior on this question, no case can be offered for the higher amount other than that it allows for possible additional ammunition cost inflation or attrition of major items.

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E.O. 12356, Sec. 3.4 (b)
White House Guide Lines, Feb. 24, 1983
By RHP NARS, Date 6/27/85

The NSC supports the State recommendation of $450 million for 1976 and $350 million for 1977. It considers this to be the absolute minimum needed to provide the required ammunition and maintenance support for Cambodian forces, while providing a small increment to permit some modest replacement of major equipment losses (e.g., tanks, personnel carriers). The continued viability of the Cambodian forces which this level will provide is a major incentive for the other side to move toward a political settlement.

The lower $400 million option in 1975 has the advantage of being close to the 1974 actual level ($412 million) and the 1975 Budget ($390 million) and estimated ($400 million) amounts, thus avoiding the need to justify an increase to the Congress.

Agency Request: Alternative #1 -- $450 million in 1976 and $350 million in 1977. NSC concurs.

OMB Recommendation: Alternative #2 -- $400 million in 1976 and $350 million in 1977. Defense concurs.

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6. Middle-East Military
& Economic Aid

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Foreign Assistance

1976 Budget

Issue #4: Indochina Postwar Reconstruction (IPR): Cambodia

Statement of Issue

What level of commodity imports is required to meet Cambodia's minimum economic requirements?

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	1974	1975 Budget	1975 Est.	1976 Alt.#1 Agency Req.	1976 Alt.#2 OMB Rec.
	($ millions)				
Commodity Import Program (CIP)	33.1	60.1	48.2	71.5	45.7
Exchange Support Fund (ESF)	18.3	17.5	9.5	17.5	17.5
P.L. 480 Freight	38.5	20.0	30.0	49.0	51.0
Refugee/Misc.	5.5	12.4	12.3	18.0	17.8
Total	95.4	110.0	100.0	156.0	132.0

The fighting in Cambodia has produced a garrison economy heavily reliant on U.S. assistance for its survival. Local industrial and agricultural production is at a standstill, requiring imports of over $200 million as compared to $97 million in 1972. P.L. 480 food aid provides the bulk of the Cambodian food imports and will be provided in whatever amounts necessary to supplement local production. The remainder of the import bill is financed by the Commodity Import Program (CIP) and by multilateral contributions to the Exchange Support Fund (ESF).

Alternatives

#1. Provide $71.5 million CIP funding, in addition to increased refugee assistance and ESF contributions (State/AID req.).

#2. Provide $45.7 million, filling the minimum requirement for CIP support, plus increases in refugee assistance and contributions to ESF (OMB rec.).

Analysis

The analysis of aid requirements assumes that the real value of non-food imports must be maintained. The average 1974-75 commodity import level for Cambodia is $80 million. After adjustment for inflation, a level of $88 million is required to maintain that import level in 1976.

DECLASSIFIED
E.O. 12356, Sec. 3.4 (b)
White House Guide Lines, Feb. 24, 1983
By DAD NARS, Date 6/27/85

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Sources of Import Financing

	1974	1975 Est.	1976 Alt.#1 Agency Req.	1976 Alt.#2 OMB Rec.
CIP				
NOA	33.1	48.2	71.5	45.7
Pipeline drawdown	20.4	3.1	2.0	2.0
ESF				
U.S.	18.3	9.5	17.5	17.5
Cambodia/Other	18.3	9.5	17.5	17.5
Total	90.1	70.3	108.5	82.7

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- Alternative #1 would exceed the $88 million import level by $20.5 million or 23%.

- Alternative #2 would fall short of that level by $5.3 million or 6%.

The $5.3 million increase in refugee assistance, contained in both alternatives, is earmarked for purchase of equipment to cultivate resettlement areas. As such, it represents commodity imports and brings the import level of Alternative #2 to $88 million, the amount required to maintain real import levels based on the 1974-75 average.

The NSC supports the $156 million level as the minimal amount which will insure Cambodian economic survival. Most of the additional aid represented by this alternative would be spent on POL and fertilizer. The NSC believes that the increased fertilizer should be retained as a part of the program; it will assist in achieving substantially increased food production which, if achieved, would reduce the requirements for P.L. 480 rice imports. OMB believes the additional amount is not needed. The demand for POL in Cambodia has declined; and food production is less a function of fertilizer than the military situation.

Agency Request: Alternative #1 - $156 million.

OMB Recommendation: Alternative #2 - $132 million.

5. Cambodia-Military Aid

Foreign Assistance

1976 Budget

Issue #6: Middle East Economic and Military Assistance

Statement of Issue

What amounts of military and economic assistance should be included in the Budget for Israel, Jordan, Egypt, and Syria?

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	1974	1975 Budget	1975 Est.	1976 Alt.#1 Agency Req.	1976 Alt.#2 OMB Rec.	1976 Alt.#3
			($ millions)			
Egypt						
Supporting assistance	--	250	250	300	250	50
Syria						
Supporting assistance	--	(75) a/	(75) a/	90	75	25
Jordan						
Grant MAP	40	100	30	100	30	30
FMS credit	--	30	30	30	10	10
Supporting assistance	46	78	78	78	35	15
Special Requirements Fund	--	100 a/	100 a/	25	25	25
Subtotal	86	558	488	623	425	155
Israel						
FMS credit	300	300	300	300	300	300
Supporting assistance	50	50	250	100	50	50
Emergency Sec. Ass't.	2200	--	--	--	--	--
Grand Total	2636	908	1038	1023	775	505

a/ $75 million of Special Requirements Fund is planned for Syria.

Background

Significant changes in the diplomatic situation in the Middle East have resulted in basic uncertainties regarding the immediate objectives of our assistance in the area.

- Negotiations have been stalled for several months.

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E.O. 12356, Sec. 3.4 (b)
White House Guide Lines, Feb. 24, 1983
By DAW NARS, Date 6/27/85

- The Arab summit conference in Rabat designated the Palestine Liberation Organization, rather than Jordan, to negotiate with Israel for return of the West Bank.

- The Arab oil producers at the Rabat conference pledged $2.3 billion annually in aid to Egypt, Jordan, and Syria in addition to the $5.3 billion pledged in the past year.

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	Cash	Other Grants	Loans	Rabat Pledge	Total
			($ millions)		
Egypt	1,320	1,650	868	1,000	4,838
Syria	640	340	224	1,000	2,204
Jordan	181	4	45	300	530
Total	2,141	1,994	1,137	2,300	7,572

These events affect the role and impact of U.S. assistance. Because the United States does not wish to signal any change from the current negotiating strategy at this time, however, the proposed assistance programs are designed to be neutral as regards signals of change.

Israel. The major unknown affecting future military assistance requirements is the U.S. response to Israel's request for $1.5 billion annually in grant aid for a ten year military enhancement program. Since the October 1973 war the U.S. has agreed to provide about $2.5 billion in arms and $2.5 billion in financing, $1.5 billion on a grant basis. An additional $300 million in military sales credits will be provided in 1975. Although there has been no economic requirement for the general balance of payments support provided to date, a continued high level of mobilization or withdrawal from the Sinai oil fields could change this.

Jordan. The United States has provided aid to Jordan to keep Israel's longest border secure and to assure cooperation in negotiations. Military assistance helps to maintain army loyalty as the backbone of a moderate regime. Economic assistance has been justified as budget support despite the country's large foreign exchange holdings. Jordan's diminished role in the negotiations and the sharply increased Arab aid have diminished the need for high aid levels.

Egypt and Syria. Economic aid to both countries is designed to indicate U.S. interest in broadening and balancing its relationships in the area, and to provide incentives to enter into those relationships. The massive assistance flows from the Arab oil producers have diminished the incentive effect, however, and reduced the diplomatic leverage of U.S. aid. Disbursed or committed assistance will meet both projected foreign exchange deficits and likely development and reconstruction activities for several years, given the sluggish administrative pace of those governments. U.S. assistance requested for 1975 will not begin to flow until 1976, due to delayed enactment of foreign assistance appropriations.

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Alternatives

#1. Increase economic aid over 1975 proposed levels and maintain military aid at those levels, with a total of $1,023 million (State req.).

#2. Maintain 1975 proposed levels, with the exception of reduced aid to Jordan, with a total of $775 million (OMB rec.).

#3. Reduce aid to levels more justifiable in programmatic terms, with a total of $505 million.

Analysis

Alternative #1:

- is designed to provide greater incentives for cooperation on a Middle East settlement.
- includes higher levels of economic aid to Egypt, Syria and Jordan, which were proposed before the extent of aid from Arab oil countries was appreciated.
- proposes levels of aid to Jordan difficult to justify in terms of that country's needs and its decreased role in negotiations.
- minimizes flexibility by raising assistance levels before we receive anything in return.

Alternative #2:

- is neutral as regards signals but communicates confidence in the established negotiating strategy.
- takes account of the diminished importance of Jordan in the negotiations and of the increased economic aid from Arab oil producers.
- does not take into account increased levels of oil producer assistance to Egypt and Syria.

Alternative #3:

- reflects changed diplomatic and economic conditions.

- takes into account the massive assistance flows from oil producer countries to Egypt, Syria, and Jordan.

- shifts our assistance strategy away from resource transfers toward a broader technical assistance orientation in which the United States has an advantage over Arab oil producers.

- shifts balance of payments support requirements onto the Arab oil countries.

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Agency Request: Alternative #1 - increase assistance over 1975 Budget level. The NSC strongly supports the State request. The levels recommended reflect the judgment of Secretary Kissinger as to the mix of U.S. participation in security and development efforts in the area most likely to encourage the parties to continue their efforts to attain a lasting peace.

OMB Recommendation: Alternative #2 - maintain assistance at 1975 Budget level, with the exception of Jordan. State's decisions on economic assistance were made before the impact of the Rabat conference, discussed above, was appreciated. (DOD concurs in the lower military assistance level for Jordan.)

7a. Phase-Out of
Military Aid Grants

FOREIGN ASSISTANCE

1976 Budget

Issue #7a: Phaseout of Military Aid Grants

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Statement of Issue

What should be the Administration's policy toward phasing out the grant military assistance program?

Background

The grant military assistance program (MAP) is in jeopardy. Among the reasons are that:

- Many country programs, begun years ago, are regarded by Congress as anachronisms.
- Major recipients are ruled by military regimes perceived by critics as oppressive.
- U.S.-furnished arms too often are used in disputes between neighbors or against a country's own people.
- Recipients are increasingly capable of supporting their forces out of their own resources.

The program, except for its training component, is no longer widely perceived as having much to do with our security in a military sense but rather as an instrument of short term diplomacy, intended to persuade recipients to do things they otherwise would not do out of self-interest, or as one element of U.S. relationships with a country. This approach militates against a coherent Executive Branch program strategy and persuasive presentation to the Congress of a clear picture of where the program is going in the future. In these circumstances, Congress has increasingly taken the initiative by cutting budget requests deeply and imposing limitations and restrictions on the program. Without an Executive Branch response to criticisms of the program that in fact sets forth a new approach to military aid, Congress will continue its recent course.

The Foreign Assistance Act has since 1963 contained a provision (Section 505(c)) requiring the termination of grant military aid to

DECLASSIFIED
E.O. 12356, Sec. 3.4 (b)
White House Guide Lines, Feb. 24, 1983
By DAD NARS, Date 6/27/85

countries able to maintain their forces without undue burden to their economies. In 1970 the Nixon Administration endorsed the general principle that MAP, except for training, be gradually phased out and replaced by foreign military sales on a credit or cash basis. In keeping with this policy, the Nixon Administration terminated grant MAP for Taiwan, Greece, and Liberia in 1973-74, but proposed to eliminate only Tunisia in 1975. This would leave a total of 21 grant materiel programs worldwide, including South Vietnam which is currently funded in the Defense budget.

In the Senate Foreign Relations Committee version of this year's foreign assistance bill, grant military aid other than training would be required to be phased out by the end of 1977, except under clearly special circumstances. The House Foreign Affairs Committee's report on the bill states that:

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> The President should take steps to implement the provisions of Section 505(c) and reduce the grant military assistance programs not only with respect to money amounts but also with respect to the number of countries receiving such assistance.

Alternatives

#1. Gradually reduce grant MAP levels and shift to FMS credit but terminate programs only for Tunisia (end of 1975) and Korea (end of 1977) (State req.).

#2. Initiate a phased shift to FMS credit beginning in 1976 and terminate all regular grant MAP programs at the end of 1977 except for countries facing active hostilities or other special circumstances (OMB rec.).

#3. Initiate a phased shift to FMS credit beginning in 1976 with the goal of ending all grant materiel programs over the 1976-1980 period except for countries facing active hostilities or other special circumstances (Defense rec.).

Analysis

Under Alternative #1, grant MAP for Tunisia would end in 1975 and for Korea in 1977. The remaining 19 country programs (nine in Latin America) would continue, though in some cases at gradually declining levels, through 1980. State and NSC believe that small amounts of grant MAP are an indispensable component of our relationships with these countries, even though they no longer make more than marginal contributions to the recipient countries' military capabilities in most cases. Several programs (Philippines, Thailand, Turkey) would be continued on grounds that MAP is essential to retain military base rights.

Under Alternative #2, Tunisia would drop out in 1975, Indonesia and nine small Latin America programs at the end of 1976, and all remaining grant programs except South Vietnam, Cambodia, and Laos at the of 1977. Other programs could be continued or added if special circumstances required, but there would be no general continuing commitment to provide grant military aid on an annual basis. In most cases, reductions in grants would be offset by increases in FMS credits.

Alternative #2 would enable recipient countries and their U.S. advisors to plan for the end of grant MAP several years in advance. Some long-term MAP recipients like Korea recognize that grant military aid will be phased out eventually, but have not been able to plan for or to prepare public opinion for its end. A planned phaseout should eliminate some of the recriminations that result from annual congressional cuts of the MAP budget request. Adoption of a planned phaseout might also improve the chances for a more favorable congressional response to Administration requests in the interim for MAP and over the longer run for military credit sales. This approach would also focus needed attention on the economic capabilities of MAP recipients and reduce the tendency to base budget requests on past program levels without regard to changing circumstances.

Base rights programs are a special category of traditional MAP programs that would be phased out under Alternative #2. A decision to terminate MAP at the end of 1977 could result in requests for an explicit rental arrangement. However, other countries where we have bases and facilities have graduated from MAP to a credit sales relationship without insisting on base rental (Iran, Greece, Taiwan), and the fact that MAP is being phased out generally should make the change more acceptable. In most cases, the United States should be able to argue that the installations serve common defense purposes and provide substantial economic benefits, or that the real quid pro quo is the U.S. nuclear umbrella or defense commitment. Some key facilities, however, serve unilateral U.S. interests and a decision will have to be made whether and how to pay for these facilities if the host countries insist on an assistance quid.

If a rental arrangement becomes necessary, there are two alternative means of financing: (1) a specific grant request, justified to the Congress in those terms, or (a) Defense funding. In either case, each program would be justified in terms of its actual purpose rather than outdated justifications associated with the traditional MAP program.

Alternative #3 represents a middle ground. It would imply an explicit Executive Branch policy of phasing out MAP over the 1976-80 period but would avoid singling out, at this time, specific countries for termination after 1977. Under this alternative (a) Tunisia would drop out in 1975, (b) programs for the Philippines, Thailand, and Indonesia would continue as proposed by State, (c) Latin American programs would be ended at the end of 1976 as recommended by OMB, and (d) MAP for Turkey and Korea would be reduced in 1976 and 1977 as recommended by OMB but without an explicit termination decision at this time. This approach would permit the use of MAP somewhat longer as an instrument of diplomacy in selected countries. However, it would be harder to implement a phaseout in these circumstances as all MAP recipients would press to be included among the exceptions.

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Agency Requests. State recommends Alternative #1 - phased shift to FMS credit but continue most grant programs (19 out of 20) through 1980.

Defense recommends Alternative #3 - phased shift to FMS credit and termination of most grant programs over 1976-80 period.

OMB recommendation. Alternative #2 - explicit policy to terminate all regular grant programs after 1977 and shift to FMS credit except where active hostilities or special circumstances warrant continued grant aid.

7b. Turkey-Military
Aid

FOREIGN ASSISTANCE

1976 Budget

Issue# 7b: Military Assistance To Turkey

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Statement of Issue

Should grant MAP to Turkey be terminated after 1977?

	1974	1975		1976		1977	
		Budget	Est.	Alt. #1 Req.	Alt. #2 DOD/OMB Rec.	Alt. #1 Req.	Alt. #2 DOD/OMB Rec.
	($ millions)						
Grant MAP	76	90	40	64	50	46	25
FMS Credit	75	90	90	115	115	135	140
Total	151	180	130	179	165	181	165
FMS Cash Sales	17	58	115	100	100	?	?

Background

Turkey, a grant MAP recipient since 1947, is economically able to purchase its military requirements on a cash and credit sales basis. The issue is the rate of the MAP phasedown and its implications for U.S. relationships with Turkey, Cyprus negotiations, and retention of U.S. installations and facilities.

The Turks on a number of occasions have attempted to make explicit the implicit linkage between MAP and U.S. facilities. The United States has regarded this as inappropriate within the NATO context. In a recent address the Turkish Prime Minister noted that a cut off of aid to Turkey over the Cyprus issue would (a) not change Turkey's policy toward Cyprus and (b) may cause Turkey to reexamine its position on U.S. facilities.

Alternatives

#1. Continue grant MAP at least through 1980. Provide $64 million in grant MAP in 1976 and $46 million in 1977, phasing down to $25 million in 1980. Provide $115 million in FMS credit in 1976, increasing gradually to $160 million in 1980 (State req.).

#2. Rapidly phase out grant MAP, terminating after 1977. Provide $50 million in grant MAP in 1976 and $25 million in 1977. Provide $115 million in credit in 1976, $140 million in 1977, and $160 million in subsequent years (OMB rec.).

DECLASSIFIED
E.O. 12356, Sec. 3.4 (b)
White House Guide Lines, Feb. 24, 1983
By DAD NARS, Date 6/27/85

	1976	1977	1978	1979	1980
			($ millions)		
Alternative #1					
MAP	64	46	35	24	15
FMS	115	135	145	155	160
Total	179	181	180	179	175
Alternative #2					
MAP	50	25	0	0	0
FMS	115	140	160	160	160
Total	165	165	160	160	160

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Analysis

Alternative #1 would phase MAP down slowly through 1980, hoping to avoid the issue of rent for U.S. facilities. This would require that the program be defended in traditional terms; i.e., defense requirements the recipient is unable to finance out of its own resources. This would appear to be perpetuating an outdated program that Congress may not support.

Alternative #2 would more sharply reduce MAP in 1976 and 1977, terminating the materiel program at the end of 1977, while providing substantially increased levels of FMS credit. The FMS credit would enable Turkey to procure its requirements without overburdening its economy and could serve as the quid for U.S. facilities following the termination of MAP, though the Turks might press for continued grant aid or some form of base "rent." The U.S. should be able to argue that the defense commitment, the nuclear umbrella, and large amounts of FMS credit are evidence of our continuing interest in Turkey. Nevertheless, should "rent" be required following the termination of MAP, the funds could be requested explicitly for that purpose.

The NSC strongly supports State's recommended levels for 1976 and 1977. NSC believes our bases and intelligence facilities in Turkey are critical to U.S. and NATO defenses in the Eastern Mediterranean, and there is strong evidence the Turks link our use of them with our grant and sales program. Our ability to influence Turkey in the Cyprus negotiations will be affected by Turk perceptions of U.S. intentions which in part will be reflected by the levels of grant aid in the near future. NSC believes a dip below the State proposed levels would risk a reaction by Turkey at the very time when its cooperation will be crucial both to the Cyprus negotiations and to our position in the Eastern Mediterranean and the Mideast.

Both alternatives involve significant reductions in MAP from levels in prior years. The amounts included in the budget for Turkey for 1976 and 1977 will be known to the Turks early next spring, but it would not be necessary to inform them of any plan to terminate grants if that were not advisable in view of negotiations over the Cyprus situation. DOD concurs in the Alternative #2 levels but would not announce a firm termination date at this time.

Agency Request: Alternative #1 -- NSC concurs.

OMB Recommendation: Alternative #2 -- Defense concurs in 1976-77 levels.

7c. Korea-Military Aid

FOREIGN ASSISTANCE

1976 Budget

Issue# 7c: Military Assistance to Korea

Statement of Issue

What level of military assistance should be proposed for Korea in 1976-1977?

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	1974	1975 Budget	1975 Est.	1976 Alt. #1 Req.	1976 Alt. #2 DOD/OMB Rec.	1977 Alt. #1 Req.	1977 Alt. #2 DOD/OMB Rec.
	($ millions)						
Grant MAP	100.0	180.0	40.0	75	50	50	25
FMS Credit	56.7	52.0	52.0	100	125	150	175
Excess Defense Articles	21.8	20.8	20.8	-	-	-	-
Total	178.5	252.8	112.8	175	175	200	200

Background

Military assistance to Korea since 1971 has been governed by a five-year force modernization (MOD) plan. Under the plan, the United States agreed, subject to available appropriations, to provide up to $1.25 billion in grant MAP, FMS credit, and cash sales through 1975. An additional $0.25 billion in excess defense articles would be provided if available.

Congress has not been willing to adequately fund the MOD plan. Through 1974, overall MAP cuts have required a shortfall in the Korea program of $306 million. In 1975, only $40 million in MAP grants is likely to be available out of the $180 million request. Consequently, the MOD plan has been extended, and approximately $400 million will need to be provided in 1976 and 1977 to complete it.

In both the House and Senate reports on the Foreign Assistance Act of 1974, violations of human rights and high economic growth rates in Korea are cited as reasons for cuts in military assistance.

DECLASSIFIED
E.O. 12356, Sec. 3.4 (b)
White House Guide Lines, Feb. 24, 1983
By [illegible] NARS, Date 6/27/85

Alternatives

#1. Modest shift to credit (State req.).

	1975 Est.	1976	1977	Total
		($ millions)		
Grant MAP	100	75	50	225
FMS Credit	52	100	150	302
Total	152	175	200	527

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#2. Accelerated shift to credit (DOD/OMB rec.).

	1974 Est.	1976	1977	Total
		($ millions)		
Grant MAP	40	50	25	115
FMS Credit	52	125	175	352
Total	92	175	200	467

Analysis

State supports alternative #1 on the grounds that higher requests are (a) of value in our relations with Korea, even if Congress is unlikely to provide funds at the requested levels and (b) are useful as cut insurance

The NSC supports State's requests. It believes that, while we are moving to eliminate the United Nations Command and to develop new security arrangements on the peninsula, we need to reassure Korea of our continued commitment to security and to stability in Northeast Asia. The requested levels would provide that reassurance and help to complete discharge of our commitment to the Korean Armed Forces Modernization Plan.

Alternative #2 includes a mix of grant and credit Congress is more likely to approve; the grant portion is more realistic and FMS credit is higher to take up the slack. It takes into account Korean understanding that high U.S. MAP budget requests will not be realized. The Korean Prime Minister has stated before the Korean National Assembly that grant MAP will probably be terminated by 1977 or 1978. The Koreans have expressed a desire for high FMS credit levels and a willingness to make substantial cash purchases to meet their military procurement needs.

Alternative #1 gives less weight than does Alternative #2 to the strength of the Korean economy. Real growth in GNP is expected to be 8-9% in 1974. Less than 4% of the GNP is spent for defense purposes. Korea is capable of handling higher FMS credit levels.

Agency Request: Alternative #1 -- modest shift to credit; provide $75 million MAP and $100 million FMS credit in 1976 and $50 million MAP and $150 million FMS credit in 1977. NSC concurs.

OMB Recommendation: Alternative #2 -- accelerated shift to credit; provide $50 million MAP and $125 million FMS credit in 1976 and $25 million MAP and $175 million FMS credit in 1977. Defense concurs.

7d. Indonesia-Military Aid

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FOREIGN ASSISTANCE

1976 Budget

Issue#7d: Military Assistance to Indonesia

Statement of Issue

How should Indonesia's improving economic outlook, chiefly due to oil revenues, affect levels of military assistance?

	1974	1975		1976		1977	
		Budget	Est.	Alt. #1 Req.	Alt. #2 OMB Rec.	Alt. #1 Req.	Alt. #2 OMB Rec.
	($ millions)						
Grant MAP	14.4	25.0	7.0	21.4	5.0	19.4	0.8 a/
FMS Credit	3.5	0	0	12.5	20.0	12.8	25.0
Total	17.9	25.0	7.0	33.9	25.0	32.2	25.8

a/ Training only

Background

Indonesia is potentially a rich country, although densely populated and in need of development. Oil, arable volcanic soil, other natural resources, and geographic location represent future promise. Indonesia's foreign exchange reserves are building rapidly to a level of $2.5 billion by the end of calendar 1974, and its oil exports will rise to $5.9 billion during this year from $1.7 billion in 1973.

Alternatives

#1. Increase total levels of military assistance in spite of growing oil revenues (State/DOD req.).

#2. Take into account Indonesia's rapidly growing oil revenues by phasing out grant MAP promptly while offering higher levels of FMS credit assistance as a gesture of continued U.S. political interest (OMB rec.).

DECLASSIFIED
E.O. 12356, Sec. 3.4 (b)
White House Guide Lines, Feb. 24, 1983
By NARS, Date 6/27/85

Analysis

Despite recent rapid growth, oil revenues and sizable foreign exchange reserves are a relatively new experience for Indonesia. In choosing Alternative #1, State and Defense prefer a wait-and-see attitude towards long term availability of petro-dollars and recommend continuing grant materiel aid indefinitely with only minimal reductions while increasing military credits.

The NSC supports the State recommended grant MAP level of about $20 million for Indonesia in 1976-77 with a gradual phaseout thereafter. The NSC believes military assistance provides a major element of political leverage because of the effective relationship that exists with the Indonesian military regime. It will be important to retain this modest program for that political purpose during the next year or two as our defense relationships are realized in the area following our withdrawal from Southeast Asia. The military aid program will be doubly important as reassurance in the wake of our termination of economic aid.

Alternative #2 recognizes Indonesia's growing oil revenues. With the limited appropriation likely to be available for grant military assistance, Indonesia is one of the countries least in need of grants. After a transitional year of $5 million in grants in 1976, Indonesia would receive grants only for training.

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	1976	1977	1978	1979	1980
			($ millions)		
Alternative #1					
MAP	21.4	19.4	19.2	16.6	14.2
FMS	12.5	12.8	11.0	12.0	13.0
Total	33.9	32.2	30.2	28.6	27.2
Alternative #2					
MAP	5.0	0.8a/	0.8a/	0.8a/	0.8a/
FMS	20.0	25.0	20.0	15.0	10.0
Total	25.0	25.8	20.8	15.8	10.8

a/ Training only

Agency Request: Alternative #1 -- $21.4 million in MAP in 1976, with no phaseout envisioned; military credit sales at $12.5 million in 1976, increasing slowly thereafter. Defense and NSC concur.

OMB Recommendation: Alternative #2 -- Phaseout of MAP, excluding training, after a transitional year of $5 million in 1976, with higher levels of FMS credit as an offset.

7e. Philippines-
Military Aid

FOREIGN ASSISTANCE

1976 Budget

Issue#7e : Military Assistance to the Philippines

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Statement of Issue

Should the presence of American military bases determine the amount and form of military assistance to the Philippines?

	1974	1975		1976		1977	
		Budget	Est.	Alt. #1 Req.	Alt. #2 OMB Rec.	Alt. #1 Req.	Alt. #2 OMB Rec.
				($ millions)			
Grant MAP	15.9	20.0	10.0	20.0	10.0	20.3	5.0
FMS Credit	8.6	5.0	5.0	7.0	17.0	9.3	20.0
Excess Defense Articles	7.0	2.5	2.5	0	0	0	0
Total	31.5	27.5	17.5	27.0	27.0	29.6	25.0

Background

The Philippine government has considered grant military assistance to be a tacit quid pro quo for the strategically important U.S. military installations at Clark Field and Subic Bay. Despite the fact that the current agreement does not expire until 1991, the Philippine government has asked to renegotiate the military relationship between the two countries at the same time economic negotiations take place. The primary motivation for negotiating both at once is that the Philippines are weak in bargaining power on economic issues and would like to use the base rent - eviction threat to bolster their position. The 1976 recommendation for military assistance will be known before these negotiations are completed and could affect the Philippine position on base rights.

Alternatives

#1. On the rationale that grant MAP is necessary to retain U.S. bases in the Philippines, request $20 million for 1976 and annually thereafter for an indefinite period (State/Defense Req.).

#2. Phase out the grant program, except for training, by the end of 1977, with a request of $10 million in 1976 and $5 million in 1977 (OMB Rec.).

DECLASSIFIED
E.O. 12356, Sec. 3.4 (b)
White House Guide Lines, Feb. 24, 1983
By [illegible] NARS, Date 6/27/85

Analysis

In recommending Alternative #1, State and Defense believe it is necessary to continue to provide grant MAP for the indefinite future to ensure retention of our bases. This view holds that these bases are of high strategic value and are irreplaceable, and that the Philippine government could decide to evict the United States from Clark and Subic in the absence of a grant *quid pro quo*.

The NSC supports the State recommendation of a straightline projection of MAP at the $20 million level for 1976 and 1977 to preclude any inadvertent diplomatic signals during the period when negotiations are being conducted involving U.S. bases in the Philippines. These bases are necessary for U.S. security, and the Philippines consider military assistance as *quid pro quo* for their use.

Alternative #2 assumes a phaseout of grant materiel by the end of 1977, offset by increased FMS credit levels. This alternative suggests that common U.S./Philippine interests, high base-connected spending (about $160 million annually), and military credit sales would provide strong reasons for the Philippines to continue U.S. access to Clark and Subic. The contrasting estimates for 1976-80 are:

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	1976	1977	1978	1979	1980
	($ millions)				
Alternative #1					
MAP	20.0	20.3	20.5	20.5	20.6
FMS	7.0	9.3	9.8	10.6	10.6
Total	27.0	29.6	30.3	31.1	31.2
Alternative #2					
MAP	10.0	5.0	0.4 a/	0.4 a/	0.4 a/
FMS	17.0	20.0	25.0	25.0	25.0
Total	27.0	25.0	25.4	25.4	25.4

a/ Training only

Agency Request: Alternative #1 -- $20 million in grant MAP and FMS credit of $7-10 million in 1976 and annually thereafter.

OMB Recommendation: Alternative #2 -- $10 million in grant MAP, phasing out grants for materiel by end of 1977, and increasing military credit sales to compensate for the phase out of grants.