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MEMORANDUM

NATIONAL SECURITY COUNCIL

ACTION
3078

~~CONFIDENTIAL~~ (GDS)

June 4, 1973

MEMORANDUM FOR: DR. KISSINGER

FROM: HAROLD H. SAUNDERS
HENRY R. APPELBAUM

SUBJECT: A Posture on Future Development
Assistance to India--Position for World
Bank Consortium Meeting June 14

Attached is a memo to the President recommending that the US not make a specific pledge of aid to India at the June 14-15 meeting of the Aid-India Consortium, but instead initiate discussions with the Indians now in an effort to work out a mutually satisfactory basis for a future aid relationship. This would give you a chance to talk with Kaul about this if you wish.

RECOMMENDATION: That you forward or authorize General Scowcroft to forward the attached memorandum to the President in time for him to make a decision as far in advance of the June 14-15 Consortium meeting as possible. (A memorandum from State/AID will recommend the approach in the attached.)

Concurrence: C. Cooper

~~CONFIDENTIAL~~ (GDS)

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MEMORANDUM

THE WHITE HOUSE

WASHINGTON

ACTION

3078

CONFIDENTIAL (GDS)

MEMORANDUM FOR: THE PRESIDENT
FROM: HENRY A. KISSINGER
SUBJECT: Aid to India

At the annual thirteen-nation aid-India Consortium meeting on June 14-15 the US will be expected to give some indication of its future plans concerning aid to India. Your FY 1974 aid proposals now before Congress provisionally include up to \$75 million for new aid to India with the clear proviso that this is still subject to your decision. The Indians are aware of this and have already been informally inquiring about our aid plans.

There are essentially three possible courses of action for the US Government. (1) not to provide India with additional aid now and not to discuss the subject; (2) to make a specific pledge of up to \$75 million at the Consortium meeting; or (3) to make no pledge at the Consortium meeting, but instead to engage in discussions with the Indians in an effort to work out a mutually satisfactory basis for a future economic assistance relationship, offering specific amounts of aid only after such an understanding has been reached.

The first option, a decision not to provide or discuss new assistance now, would constitute a strong negative signal to the Indians and would not advance our efforts to develop a sounder relationship with them. US-Indian relations have been gradually improving in recent months. The Indians have generally avoided actions offensive to us on foreign policy matters such as the situation in Indochina. Gratuitous criticism of the US by Indian politicians also has greatly decreased--in part because Mrs. Gandhi has specifically cautioned her colleagues to refrain from criticizing foreign countries. In part this "good behavior" is a consequence of India's worsening economic situation and its renewed interest in US assistance. However, the improved climate is also an outgrowth of India's belief that our present policies toward the sub-continent are more satisfactory from India's standpoint than was the

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case during the South Asian turmoil of 1971. This background of improving relations and recent more responsible Indian behavior toward us provides a basis for the step-by-step process of building a realistic political and economic relationship with India, and continued silence on the aid question will defer that process.

The second option, an immediate specific pledge, would probably be very pleasing to the Indians. I believe, however, that such an action would not be in our own interests. In the past, American aid has too often been taken for granted by India. It also has given rise to frequent misunderstanding and disagreement. To offer aid prematurely would risk reversion to this unsatisfactory pattern. Any offer of new aid should come only after there has been further progress in the improvement in our relations and a mutual understanding as to the role economic assistance is to play in our overall relationship.

The third option would be to respond to the recent Indian probes on economic assistance by initiating talks with the Indians to see if agreement can be reached on the form and purpose of aid. Such an approach would be consistent with your Foreign Policy Report, which envisages a dialogue with India to work out a mature economic relationship within which development assistance would have a role. An important aim of such discussions would be to confront the irresponsible expressions the Indians have made in the past to the effect that our aid is harmful to India. We would make clear that if the Indians view our aid as intrusive or damaging, the aid should not be provided. If our aid is desired and needed and is consonant with their values and our mutual interests, this should be understood between us, and the Indians should be prepared to say so publicly and unequivocally.

If this approach is followed, we would say at the Consortium meeting that such discussions are under way or planned and that we therefore are not in a position yet to make a specific pledge of aid. We would not make any reference to the aid bill's provisional \$75 million figure or to any other specific amount. During the next few months we would then get a better indication of Indian desires and intentions while the prospects for AID funding by Congress will also become clearer.

Most of the other donors will probably make specific pledges, and the Indians might be disappointed in our unwillingness to do so. However, they could not disregard the fact that we are willing to begin discussions on the possible role of development assistance and that we are willing to say so in an open international arena.



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RECOMMENDATION: That you authorize me, in advance of the aid-India Consortium meeting that starts on June 14, to request the Department of State and AID to initiate talks with the Indians in order to seek a mutually satisfactory basis for a future aid relationship. State and AID concur in this approach.

Approve _____

Other _____

CONFIDENTIAL (GDS)



MEMORANDUM

NATIONAL SECURITY COUNCIL ACTION

3101 (Revised)

SECRET (XGDS)

June 14, 1973

MEMORANDUM FOR:

DR. KISSINGER

FROM:

HAROLD H. SAUNDERS

SUBJECT:

Reply to a Letter and Back-channel Messages from Ambassador Moynihan

Over the past several weeks Ambassador Moynihan has sent you four back-channel messages and a letter (Tab B). This package is an update of an earlier one I sent you to include his latest. It has been revised in the light of the President's economic decisions. A draft reply to all these communications is at Tab A.

In an interim reply (Tab C) on May 14 to two of the back-channel messages, you told Moynihan you would be back in touch with further thoughts on two of the subjects raised in those messages--the idea of a US-Indian economic commission and the question of foodgrain and credits for India.

In those two messages Moynihan discussed possible Indian interest, in the face of their food problems, in seeking a resumption of US credits for foodgrain purchases. Moynihan said his personal inclination is to avoid lending them more money for food. Instead he suggests the possibility of a "straight-out or indirect barter scheme under which they pay for the wheat with goods of their own." He points out that the Indians have a barter relationship with the USSR that they seem to like.

The two messages and Moynihan's letter of May 25 also developed the idea which you have discussed for a US-Indian joint economic commission to help work out our future aid and trade relationships. The letter mentions that Ambassador Kaul will be taking this matter up with you. You will recall that Finance Minister Chavan thought perhaps US-Indian economic issues should be handled informally for a time.

XGDS - 3

DECLAS - Date Impossible to Determine.

BYAUTH - Dr. Henry A. Kissinger

SECRET (XGDS)

DECLASSIFIED

AUTHORITY state dept. sec 9114/03

BY dal NLF, DATE 7/6/09



Handwritten notes and signatures: "Bushnell", "Cooper", "JFK", "Tab A", "and send", "Kaul".

On food and aid, the draft reply to Moynihan takes into account current uncertainties in the foreign aid picture, the tightness of foodgrain availabilities for export, and the President's June 13 speech on the economy.

I would suggest handling the question of the joint economic commission this way: Some weeks ago entirely independent of your discussions with Moynihan, I asked State to do a study of where our non-aid economic relations with India are going. We should have this study shortly. That will give us a bureaucratic foundation on which to build. In short, it seems to me that it may be wise to deal with outstanding economic issues one at a time and then to see whether some sort of commission might be useful in overseeing the implementation of unique US-Indian agreements. This would avoid setting up a commission before assuring that it could achieve results.

Moynihan's two more recent back-channel messages concern USG negotiating terms in the forthcoming bilateral negotiations on excess rupees. Moynihan has been informed by Sisco about the negotiating instructions contained in an interagency package that has been approved by most of the bureaucracy and is now before Secretary Shultz for his signature. Moynihan feels the terms contained in the package are too hard and he hopes you will soften them. We should be getting the package from Secretary Shultz within the next few days, at which time we will be giving you our recommendations on the matter. The proposed message to Moynihan at Tab A tells him we are presently awaiting the package, and also points out that Congressional attitudes have to be taken into account.

RECOMMENDATION: That you approve the message at Tab A for transmission to Ambassador Moynihan.

Approve _____

Other _____



Concurrence: C. Cooper

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WITHDRAWAL ID 027827

REASON FOR WITHDRAWAL ÇNational security restriction

TYPE OF MATERIAL ÇTelegram

CREATOR'S NAME Henry A. Kissinger

RECEIVER'S NAME Ambassador Moynihan

DESCRIPTION Draft message re US-Indian economic relations

CREATION DATE 06/18/1973

VOLUME 5 pages

COLLECTION/SERIES/FOLDER ID . 034100024

COLLECTION TITLE NATIONAL SECURITY ADVISER. NSC
INTERNATIONAL ECONOMIC AFFAIRS STAFF
FILES

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FOLDER TITLE Country File - India

DATE WITHDRAWN 01/10/2007

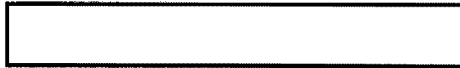
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June 18, 1973

TO: NEW DELHI (AMBASSADOR MOYNIHAN/EYES ONLY)
FROM: THE WHITE HOUSE/HENRY A. KISSINGER

1. I have in hand your letter of May 25 regarding a US-Indian joint economic commission, your two earlier messages which dealt with the commission idea and other subjects, and your two recent messages on rupees.

2. Economic issues, as we have said before, will now tend to become more important in the Indo-American dialogue. As I look more closely at these issues, it occurs to me that at this point in talking with the Indians we might do well to avoid trying to move too fast. For instance, we may want to avoid being very specific or very optimistic about aid. First of all, before we start getting into specifics on aid we need to develop further understandings with the Indians about where our relations are going and how aid fits in. These discussions can begin soon. Second, at present the availability of grain for all programs involving USG-financed exports or even commercial exports is very tight, and the picture for foreign aid in general is uncertain. Maybe the aid picture will look better a few months from now, but that is by no means assured.

Handwritten notes:
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... State Review 9/11/83
... NSC memo, 11/24/88
... DATE 4/12/87

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SECRET (XGDS)

- 2 -

I think we should avoid getting Indian hopes up too soon on aid. On the grain problem, in following up the President's June 13 announcement about limiting food exports we probably will soon be consulting in detail with the Indians and other importing countries. You might want to consider how these discussions will fit into the overall Indo-US dialogue in view of the fact that our message on grain will be much less helpful than we would like. On some of the other issues, I think we will want to look at what can be achieved. Kaul, with whom I lunched Friday, shares these views. I will send you a full report in a few days.

3. Ambassador Kaul believes the Joint Economic Commission should phase out after rupee discussions. Some weeks ago we encouraged the State Department to prepare a rather comprehensive study on US-Indian economic issues and possible mechanisms for dealing with them. This study should be ready in a week or two and should provide a bureaucratic foundation for developing the idea. I tend to agree with Kaul's views.

4. If we proceed along these lines, there should at least be the opportunity over the next few months to initiate several more or less separate sets of bilateral discussions with the Indians on different economic subjects--i. e., the talks on rupees; on trade and investment; on scientific and technological cooperation; and on an aid relationship.

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- 3 -

Since some of these may not move quickly or lead to easy or obvious conclusions, it may be that the best time to set up any special mechanism would be after some agreements have been reached on the above subjects. This means that an economic commission of some sort could be considered once there are some agreements that the commission could oversee and help to implement. It now seems to me that this approach--as opposed to going for early establishment of a commission--might help avert two pitfalls: the danger of setting up a commission that proves unable to accomplish anything, and the danger of having all sorts of other countries wondering aloud why we are singling out India for a joint commission.

~~Of course, these are just current thoughts. I will want to see what Kaul and others have to say before I reach any firm conclusions. I will keep you abreast of how this evolves. It is clearly important to get maximum political benefit out of any of these steps and that is where your careful handling will come in.~~

5. One of your messages discusses the idea of a barter scheme involving US foodgrains for Indian goods. I suspect there would be some formidable difficulties with this. In the first place, foodgrains for export will be scarce for a year or so. Beyond that, there are complexities involved in trying to set up something like this in a private economy such as ours.

SECRET (XGDS)



SECRET (XGDS)

- 4 -

Also, there would presumably have to be some way of doing it so that the Indians could get more food through such an arrangement than they could buy with the foreign exchange that their commodities would otherwise earn. This, it would seem, would mean some sort of subsidy arrangement-- in effect, food at least partly on an aid basis.

6. Another approach--a bit farther out--might be to sound out the Indians and US industrial investors on the idea of investors obtaining foodgrains and supplying them to India, in return for which the Indian government would agree to do such things as pick up some of the investors' local rupee costs and in general ease obstructions to US private investment there. Possibly some sort of foodgrains-now-for-ore-later concept could be explored with the Indians and with US mining investors.

7. I am sure there are plenty of problems with these notions, and maybe they could not involve enough food to make much difference. In any case, they do not seem as promising now as one would have hoped because of their complexity and because of our own problem with grain supplies.

8. These thoughts on barter, which I suspect are not at all new, are based on nothing more than some informal thought here and obviously would require a lot of further exploration inside and outside our government. You may want to have your staff try some of these ideas out on their colleagues here.

SECRET (XGDS)



~~SECRET~~ (XGDS)

- 5 -

9. On rupees, we are still waiting to receive the interagency package. As of right now it has gone through most of the bureaucracy and is in the hands of Secretary Shultz. It should reach the White House within the next few days. When it does we shall have your messages before us as we examine the problem. We also have to concern ourselves with the danger of a negative Congressional reaction to a "giveaway" which could have an adverse effect on pending legislation such as the foreign aid bill.

Warm regards,

~~SECRET~~ (XGDS)





DEPARTMENT OF STATE

Washington, D.C. 20520

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July 24, 1973

LIMITED OFFICIAL USEMEMORANDUM FOR MR. HENRY A. KISSINGER
THE WHITE HOUSE

Subject: Indo-US Economic Relations

In his 1973 Foreign Policy Report the President spoke of the need to develop a new framework for Indo-US economic relations. The attached memorandum, reflecting the views of State, Treasury, Commerce, AID and NASA, outlines our thinking on how we should approach this task.

In brief, we propose an economic framework that places greater emphasis on trade and commerce and moves away from the patron/client relationship that has existed since large-scale US bilateral aid began in the 1950's. We see the economic dialogue encompassing five main areas: rupees, economic assistance, trade expansion, investment, and scientific and technical cooperation. Ambassador Moynihan and our Mission in Delhi will serve as the focal point for on-going discussions/negotiations on these topics with the Indians. In the talks, we would emphasize that we see the individual issues linked together as part of an overall effort to shape a new economic relationship.

We think that sufficient trade-offs exist of interest to both the US and India to offer reasonable prospects of achieving more balanced economic relations. This approach will reinforce the parallel effort under way to shape more realistic political relations based on mutual respect and mutual understanding.

Theodore L. Eliot, Jr
Executive Secretary

Attachment:

Memo on US-Economic Relations

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Indo-US Economic Relations

In his 1973 Foreign Policy Report, the President spoke of the need to develop a new framework for Indo-US economic relations over the longer term. This memorandum outlines our thinking on how we should approach the task and what elements should be encompassed within the framework.

1. Overall Approach

-- We should seek a more mature and business-like economic relationship with India, just as we are trying to achieve sounder and more realistic political relations.

-- Our objective would be the working out with India of an overall economic relationship that emphasizes trade and commerce.

-- Essentially, this means greater stress on reciprocity in the place of the patron/client relationship that has characterized our economic ties since large-scale US bilateral assistance began in the mid-1950's.

-- At the same time, we would broaden our discussions with India on major international economic issues. As a Third World leader, India has an important voice in consideration of monetary and trade policy questions in the multilateral arena.

2. Rationale for the New Framework

-- The donor/recipient relationship that existed before 1971 grated Indian sensitivities and brought us only limited benefits. It would be a mistake to return to this unsatisfactory situation; a new approach is needed.

-- Despite disparities in the size and nature of our economies, a basis exists for less one-sided and more reciprocal economic intercourse.

-- With 40% of Indian imports handled directly by government corporations and 100% subject to administrative controls, there is ample scope for the Indian Government to affect the pattern of foreign purchases.

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-- Despite uneven economic performance, India has a GNP of \$63 billion, which makes it the world's 10th largest economic power. Indian imports exceed \$2 billion. In 1972 the US share, including aid-financed goods, was only \$350 million. Our traditional favorable balance of trade was replaced by a \$100 million trade deficit. There is scope for trade expansion.

-- In terms of economic trade-offs, both we and the Indians have things wanted from the other side:

-- We want greater opportunity to share in the Indian market, especially for high technology communications and transportation goods; we want removal of administrative barriers to US exports; we want to be able to tap Indian scientific brainpower for joint research projects.

-- India wants a settlement of the rupee problem, a renewal of bilateral aid, greater technology transfer from the US and increased exports to the US.

3. The Specifics

We see the need to focus our economic dialogue on five principal areas: (a) the rupee problem; (b) economic assistance; (c) trade and commerce; (d) US investment in India; and (e) scientific and technical cooperation. There will be scope for greater specificity on each of these once the dialogue gets underway; our current views are as follows:

(a) The Rupee Problem

-- Our present and potential rupee holdings (\$3.2 billion equivalent plus interest), a product of our economic assistance relationship, have become a major problem that needs to be solved before we can attain mature economic relations. Negotiations on rupees have commenced in New Delhi.

-- The object of a rupee settlement will be to remove Indian psychological concerns about our large holdings of their currency while at the same time protecting our right to pay for USG expenses in India with rupees rather than dollars for an extended period.



(b) Economic Assistance

-- Beginning in 1946, the US has provided India \$9.2 billion in bilateral assistance. Of this, \$2 billion was on a grant basis and the rest was either on dollar or rupee repayable terms. \$1.6 billion has already been repaid; a rupee settlement will reduce the debt to about \$2.7 billion, primarily from aid development loans.

-- 1971 marked a watershed. The Indians ended Title I PL-480 foodgrain programs. Title II programs have continued, averaging \$50 million a year, but the Indians hope to phase these out in the next few years. 1971 also saw the US suspend development loans. While the suspension on \$87.6 million was lifted in March 1973, we have made no new loans since then.

-- In the same period, indirect US lending to India through multilateral channels, principally the International Development Association, substantially increased. In effect, transfer of US capital resources for Indian development has shifted from bilateral to multilateral channels. A reduction in India's share of IDA loans, currently 40%, is likely to occur to permit expanded IDA lending elsewhere, especially in Southeast Asia. We have supported this move. With an anticipated increase in IDA lending in the fourth replenishment period, a smaller Indian share would not cut the absolute level of loans to India.

-- At this time, the future of US bilateral assistance is uncertain. Any renewal would clearly be unwise unless past problems can be resolved, particularly Delhi's willingness to accept aid almost as a right while at the same time complaining that in some way our help harms India.

-- In 1974, we will face an important economic policy question in responding to India's request for a five-year debt relief plan. We have participated in five multilateral debt rescheduling exercises even though we have been dissatisfied with certain aspects of them.

(c) Trade and Commerce

-- We would explore with the Indians how to increase our trade in ways that benefit our respective economies.



-- We would be willing to consider an Indo-US "trade agreement," about which Indian Planning Minister Dhar has spoken, if this can result in increased trade for both sides without violating GATT obligations.

-- We would also be willing to consider a Friendship, Commerce, and Navigation Treaty as a means to promote trade.

US Exports

-- India offers limited short-term trade prospects for US business, but its long-range potential is substantial and warrants a sustained export development effort. The USG will need to explore ways to assure competitive financing for US exports. This may be facilitated under the new aid legislation under consideration by Congress.

-- The USG would increase its support for specific sales proposals by US companies. For example, current efforts to sell more airplanes (Boeing) and communications satellites (Fairchild Industries). We could also explore expanded contacts with Indian state trading concerns, which are playing an increasingly important role in Indian trade.

-- The USG would expect action by the GOI to remove administrative or trade control practices that seem to discriminate against US companies.

Indian Exports

-- In our current trade legislation, we seek authority to introduce generalized preferences for developing countries, a proposal in which India has a substantial interest.

-- Depending on Indian entrepreneurial skills, there would appear to be scope for increased exports of non-traditional products such as light manufacturing goods to the US, especially if the developing countries receive trade preferences.

(d) Investment

-- The USG will vigorously support claims of nationalized US concerns, such as those presented by the six US insurance companies, for just, prompt and effective compensation.



-- Given the Indian Government's negative attitude toward many types of foreign investment, there is limited scope for expansion of traditional investment-- and relatively little interest on the part of U.S. industry. Total US private investments in March 1973 were only \$329 million, small in comparison with the size of the Indian market.

-- As a way of spurring increased trade, new approaches to investment are, however, worth exploring, including minority partnerships with Indian public sector companies and barter-type arrangements where US know-how capital is offset by export of raw materials.

(e) Scientific and Technical Cooperation

-- Both sides have expressed a desire for continuing scientific and technical cooperation, but there are problems.

-- The Indians have almost entirely terminated the AID technical assistance programs while continuing to affirm their desire for expanded technological cooperation.

-- USG agencies have stated their continuing interest in joint research projects that tap Indian scientific brainpower and are funded by US-owned Indian rupees. The Indians have, however, refused to approve new projects since July 1972. Annual expenditures have been running about \$6 million equivalent.

-- The solution would appear to lie in the development of more mutually satisfactory mechanisms. We would seek Indian views in this regard; an overall understanding on scientific and technical cooperation would seem to be desirable.

-- We should explore bilateral cooperative agreements in areas of specific interest and non-military in character, for example, domestic telecommunications. Such an approach could also be helpful in facilitating US exports such as the proposed \$100 million follow-on to the NASA/GOI educational TV satellite experiment.

4. How We Would Proceed

Ambassador Moynihan and the Embassy in New Delhi will serve as the focal point for on-going discussions with the Government of India. In presenting USG views,



we would emphasize that we considered the individual issues linked together as part of the larger effort to develop an overall and more reciprocal economic relationship.

-- If the discussions proceed satisfactorily and there are concrete achievements, we could consider symbolizing the new economic relationship by establishing a joint economic commission or some similar mechanism, about which the Indians have expressed interest.

5. What are the Prospects

-- Although the proposed approach breaks with past practice, we gauge the chances for achievement of substance as reasonably good.

-- Both we and the Indians have called for a new relationship with greater emphasis on trade, not aid.

-- We see economic trade offs of interest to both countries.

-- There does appear to exist a greater basis for reciprocity in our economic dealings. A case in point is our current offer to India of a larger quota for textile shipments to U.S. in return for Indian support for the multi-fibre textile agreement.

-- The proposed approach reinforces the parallel process begun in the political sphere of trying to develop a more mature and realistic Indo-US relationship.



Mr. Cooper

Bush
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CONFIDENTIAL (GDS)

July 31, 1973

MEMORANDUM FOR: DR. KISSINGER

FROM: HAROLD M. SAUNDERS

SUBJECT: Your Meeting with Indian Finance Minister Chavan--12:30 p.m. Wednesday, August 1

Chavan is here for a Committee of 20 meeting. Since you last talked with Chavan in October about how we might proceed with a US-Indian economic dialogue, Ambassador Moynihan has gone to New Delhi and is now embarked on three aspects of that dialogue:

1. Rupees. Moynihan has begun negotiating. He reports that his trickiest problem lies in explaining the undesirability of setting a fixed period of years for the expenditure of the "US Trust Fund," as the US-held rupees are being held. He is trying to argue for a fixed sum rather than a fixed time period. He anticipates an agreement by early September.

Your point: It seems to me you will want to avoid expressing a view on specific issues now. Your basic contribution has been to bring our opening position to a point where it offers a realistic basis for negotiation. You can take credit for that but go on to argue that it is your practice not to bargain but to present an opening position close to the one you hope to end up with. The point to be stressed is that this issue has the potential of arousing significant Congressional opposition and that there are, consequently, certain things that we will need. They are reflected in our opening position--for instance, more than a token retention of rupees to fund US operating expenses--and the Indians should recognize that there are real limits below which they cannot push us if they want an agreement. [This figure is around \$1 billion, but it would be desirable to leave the figures to Moynihan in order not to undercut him.]

CONFIDENTIAL (GDS)

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2. Economic assistance. Moynihan has said he is prepared to discuss future cooperation on economic development, and Foreign Minister Singh has said we could take India's interest in such assistance as "given." Singh seems to be trying to avoid a situation in which India has to ask for aid. What needs to happen now is for two people who understand the development business to talk through what a sensible development program avoiding potential irritants on both sides would look like. There is no urgency about this, but only when those conversations have taken place will we have a basis for an Indian acknowledgment that such aid would serve Indian interests.

With the likely cuts in our aid appropriations this year and budget constraint for FY-75 we can make substantial funds available to India only by cutting back elsewhere. With the requirements of Indonesia, Pakistan, Korea and Indo-China and major cuts in the PL 480 program because of commodity shortages, there is little room to cut. Our FY-74 request which is public contains \$75 million for India but we will probably be cut by far more than this \$75 million. Thus we should not encourage the aid dialogue to move very fast.

Your point: You might say that Ambassador Moynihan is prepared to talk and that what seems needed now is a discussion of what kinds of cooperation would be mutually acceptable. This will have to be a talk between those who are able to deal not only with the technical questions of what would make economic sense but also with the broader questions of what is politically acceptable. You might add, however, that our Congressional problems will make resumption of substantial concessional aid very difficult.

3. Trade. Moynihan is committed to talk about trade, but his exchanges to date have been only very general. Moynihan is also telling the Indians they ought to re-think their attitude toward American private investors now that even the USSR is seeking a close relationship with American firms.

Your point: You might simply say that trade is a difficult area for us because of domestic interest groups. However, we are willing to make an effort to increase trade both ways.



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- 3 -

In short, your main purpose is to give White House endorsement to the economic dialogue that is beginning and to urge that this be seen in India as a concrete indication of US interest in improving relations with India. You might ask for his views on where we stand.

On the question of grain, the Indians were told that they were free to buy and that if they acted energetically, they could probably buy three or four million tons. Our latest count indicates that they have ordered about a million tons so far.

You will want to recall that you promised to arrange a meeting for Kaul with the President about now. I am sending you a separate schedule proposal for that.

Concurrence: C. Cooper

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HHSaunders:JAB:tmt 7/31/73



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DEPARTMENT OF STATE

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Washington, D.C. 20520

September 11, 1973

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MEMORANDUM FOR BRIG. GEN. BRENT SCOWCROFT
THE WHITE HOUSE

Subject: Transition--Congressional Consultation
on Rupee Negotiations with India

In his testimony before the Senate Foreign Relations Committee this morning Secretary-designate Kissinger was asked about the status of the rupee negotiations currently being conducted with India and plans for consultation with the Congress. A memorandum discussing the subject is attached.

Thomas R. Pickering
for Thomas R. Pickering
Executive Secretary

Attachment:
Memorandum on Rupee
Negotiations

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Status of Rupee Negotiations and Congressional Consultations

Ambassador Moynihan reports that Prime Minister Gandhi has just accepted our basic proposal for a rupee settlement. If President Nixon concurs, an agreement ad referendum could be initiated in Delhi soon. In consultation with other Executive Departments, we plan to forward our recommendations promptly to the President.

The main features of the proposed agreement are:

-- The US will retain for its unrestricted use in India (and Nepal) \$1 billion equivalent of rupees. This sum should cover all USG expenditures for about 15 years.

-- The remaining funds (approximately \$3.5 billion) will be disposed of through our foregoing interest payments and our granting to India for our mutually agreed economic purposes approximately \$2.2 billion.

-- The Indians are giving us:

- additional hard currency conversions or direct dollar savings worth approximately \$70 million;

- concessions on our continued use of rupees in Nepal.

The rupee agreement will not require Congressional approval. We have authority, under PL-480, to make the grants contemplated above. AID and Treasury General Counsels have determined that we may accept Indian prepayment of outstanding rupee loans and that we may hold the deposit balances we retain in non-interest bearing accounts.

However, the two provisos of PL-480 which permit us to make grants, without appropriation, to India require respectively:



-- that for about \$2 billion of the grant we inform the respective chairmen of the Agriculture Committees (these grants would be made under the Mondale-Poage proviso of PL-480, Section 104);

-- that for the remaining \$200 million, we table the proposed grants with the Agriculture Committees for thirty days while Congress is in session (these grants would be made under the Presidential waiver proviso of PL-480, Section 104).

From the outset we have felt it essential to consult closely with the Congress. Before negotiations began, we met with appropriate members of Foreign Affairs/Relations and Agriculture Committees (Messrs. Fulbright, McGovern, Talmadge, Poage, and Hamilton). Members of the Appropriations Committee were informed by AID officials during the testimony on the FY-74 AID bill.

Our judgment, following this first round of consultations, was that the Congressional problem was manageable, but only if we continued to keep in close touch.

We intend to have a second round of consultations with Congress as soon as the President approves the main principles of the agreement reached in Delhi. Ambassador Moynihan is willing to take the lead in these consultations. We attach a paper prepared for use on the Hill.

Ambassador Moynihan has made clear to Mrs. Gandhi that any agreement would be subject to satisfactory consultations with the Congress.

Attachment:
Rupees Paper



INDIAN RUPEES

-- As part of our effort to develop a mature economic relationship with India, we are negotiating ultimate disposition of US claims on Indian rupees.

-- These Indian rupee assets consist of \$840 million equivalent in current US deposits in India's central bank and \$2.4 billion equivalent in outstanding principal on loans owed to us over the next 40 years. With interest, rupees come in at over twice the annual rate at which we spend them.

-- The bulk of the claims come from the proceeds of PL-480 agreements for foodgrains concluded between 1957 and 1971. The remainder are from rupee-repayable dollar loans made in the 1950's to support India's economic development.

-- The original aid agreements limited the use of rupee assets, largely to cover US expenses in India and to relending for Indian development.

-- The General Accounting Office in its 1971 report to Congress noted that the US could not expect, as a practical matter, to be able to spend more than a portion of the rupees.

-- Our aim is a more realistic and more healthy situation. We expect to gain renewed assurance that we can continue to use rupees rather than dollars to cover our expenditures in India for an extended period.



-- Any rupees returned to India as a result of a settlement would be clearly in excess of our needs.

-- Authority to grant or loan excess US-owned foreign currencies to foreign governments is contained in section 104 of the Agricultural Trade Development and Assistance Act of 1954, as amended (PL-480).

Such authority is adequate to resolve the excess rupee problem in India.

-- It is not proposed that rupees generated by non-PL-480 agreements be granted to India. They would be retained for United States Government uses.

We have proposed the following to India:

-- That we retain \$1.1 to \$1.5 billion equivalent in a dollar-denominated interest-free account in India's central bank for our exclusive use in India and Nepal.

-- That we draw down this account for as many years (estimated at 15 to 25) as necessary to spend all the money.

-- That we grant the remainder to India for mutually agreed economic development activities and the creation of endowment funds to finance mutually agreed programs. (None of these programs would relate in any way to military or defense activities.)

-- That we receive additional conversions of our rupees into hard currencies above amounts previously provided for.



-- That we retain complete control over our use of our rupees for the full range of purposes and programs hitherto so financed (i.e., all USG expenditures in India, including congressional travel).

-- That we resume funding with Indian rupees the local costs of our AID program in Nepal, as well as continuing to use Indian rupees in support of all other USG programs there (e.g., State, USIS, and PC).

-- That the Indians provide us maintenance of value on the rupees reserved for our use to protect us against any future devaluation of the Indian rupee.

-- We plan, of course, to report further to concerned committees of Congress.



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MEMORANDUM FOR: SECRETARY KISSINGER September 28, 1973

FROM: HAROLD H. SAUNDERS
CHARLES A. COOPER

SUBJECT: Ambassador Moynihan's Paper on Possible
US Initiatives Toward India

This memo summarizes and comments on Ambassador Moynihan's recent memorandum to you outlining possible US initiatives toward India. Moynihan's memo is at Tab A. We are sending this to you now in case you should be seeing Moynihan before the end of the week. Moynihan is in Washington now and will be here until Saturday when he leaves for India with a stop in Japan.

Moynihan groups some two dozen proposals into three categories: Atmospheric, Political Support, and Economic Support. He lists the advantages and disadvantages of each proposal. He comments that "in general, the balance of the argument is with the disadvantages." He adds that US-Indian relations have already been restored to a "correct level of cordiality" and that right now the USG should wait to see how the Indians respond to initiatives we have already taken, such as Embassy New Delhi's aide-memoires on aid and trade relations, before taking any more new initiatives. We (Saunders and Cooper) agree with that judgment.

(Of the several recent US aide-memoires submitted to the Indian Government on economic matters, the only one the Indians have replied to is the one on rupees. A proposed rupee agreement that the Indians appear willing to sign is now making the interagency rounds in Washington. Moynihan has been meeting with top officials of all the agencies concerned as well as with key Congressmen and Senators in order to smooth the way for the proposed agreement, and it will be arriving here soon for the President's approval.)

In Moynihan's paper, the possible initiatives listed under "Atmospherics" include a continuing Nixon-Gandhi correspondence, a joint Indo-US statement of principles to govern relations, and visit to India by the President, yourself, or Secretary Shultz. The joint statement and/or the visit

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could be timed to coincide with the signing of a rupee settlement. A drawback common to all three of these proposals, as the Moynihan memo itself points out, is that their contribution to better Indo-US relations would probably be very perishable unless we were in a position to follow up in some concrete way in political or economic matters of importance to India. By and large, as is pointed out below, we do not appear to be in such a position right now.

The eleven proposals listed by Moynihan under "Political support" include five which appear to conflict with important US policy objectives vis-a-vis other countries. The five are:

- Selling arms to India.
- Offering India more explicit assurances regarding non-transfer of arms from Iran to Pakistan.
- Promoting a permanent Indian seat on the UN Security Council.
- Supporting a more prominent Indian role in Southeast Asia.
- Issuing a statement highlighting our willingness to do business with the subcontinent in terms of India's preeminent position there.

Two of the other proposals in the political category would involve the USG's making official statements that would make it harder for us subsequently to disagree with the Indians when their and our interests diverged. The two are:

- Telling the Indians we plan to support them more on international issues.
- Issuing a statement indicating India's importance in the Indian Ocean and our willingness to cooperate with India on matters such as the Indian Ocean Peace Zone proposal and US fleet movements and bases in the area.

Moynihan also suggests that the USG encourage the Chinese to improve their relations with India. This seems like a reasonable idea to us but it may well be inconsistent with the broader approach we have shared with the Chinese and with higher USG priorities regarding China. Another

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proposal in Moynihan's paper--resumption of the Indo-US bilateral talks conducted in the late 1960s--would probably not serve much purpose (and might even have a negative net effect on relations) unless there were specific matters that could best be handled through such talks. Moynihan's paper points out that these bilateral talks have generated more heat than light in the past and that the issues they might deal with can be handled just as well by the US Ambassador in New Delhi.

Moynihan also considers an Indo-US Friendship/Commerce/Navigation Treaty. We believe this would be viewed with concern by Pakistan and perhaps other neighboring countries. It also might appear as little more than a transparent effort on our part to match or offset India's 1971 friendship treaty with the USSR. To the extent that the USG envisaged such a pact as emphasizing trade and investment rather than the political and security factors emphasized in the Indo-Soviet treaty, a US proposal to India for consideration of such a treaty ought to be based on some good indications that there really are strong possibilities for increasing bilateral trade and investment. Such indications are presently lacking.

Moynihan's final suggestion in the political category--an Indo-US cultural exchange agreement--seems unobjectionable to us.

Moynihan's list of ten possible economic measures does not offer much promise. Four of the proposals would require US treatment of India on a more favorable basis than other developing countries, including those such as Pakistan and Indonesia with which we have basically closer ties. The four are:

- US Government guarantees of private investment under special conditions set by the Indians;
- USG payment of royalties and other costs of technology transfer;
- a joint Indo-US economic commission;
- a special joint program for Indian agricultural self-sufficiency.

Some of the other economic proposals involve international negotiations where what is proposed would represent a major change in US policy in order to accommodate India and others:



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- US support for the SDR link with aid;
- support for India's position on international trade and tariff issues;
- taking the lead in supporting an FAO proposal for establishing emergency food stocks, including a major storage facility in India.

The last proposal is one we shall be investigating further as we pursue the work initiated by the Agriculture NSSM (187), but this will be part of a worldwide program and may not get us much credit with India.

Finally, Moynihan considers an agreement to prevent double-taxation, and two bilateral aid measures--a large one-time grant of fertilizer and a \$75 million FY-74 development loan. The double-taxation agreement would give us no problems, but Moynihan concludes there isn't much in it for the Indians who do not want imports or investment from the US.

The fertilizer proposal would be particularly difficult because of the serious shortage of fertilizer in the US which is expected to last for at least another year. With expected Congressional cuts in our aid request this year, coupled with the reduction in PL-480, we shall be hard pressed to meet the most critical needs of such countries as South Vietnam and Indonesia which depend heavily on us for assistance. The largest aid program we could provide India would be tiny in relation to its needs, to its economy or to its assistance from other donors. At any rate, Moynihan concludes that such a bilateral program would get us back to the old style of aid and US-India relations and overturn our present strategy of developing a more mature relationship.

While there are problems with the bilateral aid proposals in Moynihan's paper, US support for replenishment of IDA at the higher level of \$1.5 billion per year (one-third from US) would give India major concessional assistance. Even if India's share of IDA is reduced from the current level of over 40 percent to about a third in order to facilitate IDA lending to Indochina, India would get more funds annually than it has been receiving from IDA. Moynihan might wish to emphasize the US role in IDA with the Indians. It is obvious that the \$500 million a year India would get from IDA dwarfs the \$75 million we have requested from Congress for a bilateral program.

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In short, we would argue against making dramatic gestures now in an attempt to accelerate the improving trend in US-Indian relations. Many of the proposals listed by Moynihan conflict with other demands on US resources or other US policy goals. Some of the proposals run the risk of turning out to be essentially empty gestures that would not do any lasting good for US-Indian relations, and in fact could lead to the kind of unrealistic and unfulfillable expectations which have damaged relations in the past.

We think that the best approach is the present, undramatic one of offering to engage in discussions with the Indians in New Delhi to see what prospects there might be for expanding our economic relationships. Although most USG analysts do not believe that the prospects are very good for substantially expanding US trade with and investment in India, talks on these matters with the Indians should at least serve to pinpoint where the obstacles lie; and would probably strengthen our ability to rebut Indian arguments that the obstacles are largely on our side. Our offering to have such discussions demonstrates to the Indians that we are giving serious attention to improving the bilateral relationship and that we are trying to go about this in a realistic and concrete way.

Although this sounds somewhat negative, the rupee agreement is a milestone and will take most of the rest of this year to complete. It seems a reasonable approach to ride the back of that agreement for some months before looking for anything new of major proportions.



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REASON FOR WITHDRAWAL ÇNational security restriction

TYPE OF MATERIAL ÇMemorandum

CREATOR'S NAME Daniel P. Moynihan

CREATOR'S TITLE Ambassador to India

RECEIVER'S NAME Henry A. Kissinger

RECEIVER'S TITLE Secretary of State

TITLE Possible American Initiatives Toward
India

CREATION DATE 09/05/1973

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MEMORANDUM

September 5, 1973

TO: Dr. Henry A. Kissinger
Secretary-designate

DECLASSIFIED w/ portions exempted
E.O. 12958 (as amended) SEC 3.3
MR # 09-63 #9

FROM: Daniel P. Moynihan
Ambassador to India

CIA RU 1125110; State RU 214/110
By DLJ NARA, Date 3/7/10

SUBJECT: Possible American Initiatives Toward India

Here is the list of possible American initiatives toward India for which you asked. They are grouped under Atmospherics, Political Support, and Economic Support. The Advantages and Disadvantages of each move are summarized.

In general, the balance of the argument is with the Disadvantages. (One exception: A visit by you or George Shultz to sign a rupee agreement.) This outcome corresponds closely -- as presumedly it ought -- to a Six Month exercise we carried out in mid-August, asking how we were doing, with a special prize for the nastiest answer. The consensus was that we are doing all right enough, that we have restored relations to a correct level of cordiality, and that we have genuinely impressed the Indians with our desire to create a new and enduring relationship. However, we do not think we have got across any concept of what a new relationship might be other than a version of the "old," idealized relationship of the early 1960s. This is not altogether our fault. Indians have but little feel for American realities. But it is nonetheless partly our fault. From the time I arrived we have been going to the Indians with proposals for things we might do together. We have been tough, even brutal about actions and statements on their part which do not please us.

[Redacted]

But still, it is we who have presented aide-memoires on rupees, on development assistance, on trade expansion, ^{etc.} So far, they have not responded to any save the rupee proposal. Accordingly, toward the end of August we adopted a policy ^{of} taking no further initiatives. It is now, we feel, their move.

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I would call attention, however, to a new American role in India, that of Creditor. Over the next five years, Indian dollar debt service paid to the United States will average \$130 million per year, 30 percent of their earnings from exports to the US. I see no way for us to avoid becoming a net recipient of Indian aid (sic) unless we go in for debt rescheduling on a large scale, a move Treasury will understandably resist. (The administration envisaged \$75 million in development loans for India this year; the Senate has approved \$28 million for the world. The West Germans will give ~~India~~ \$126 million this year, three to four times as much aid to India as we are likely to provide.) We can and will argue that we contribute through the World Bank and other such institutions, but it will be a tough point to make. We think a balance of payments crisis is at least a possibility. (Everyone else in Delhi thinks it inevitable.) I would anticipate a general move for a debt moratorium or even debt repudiation. In the meantime ^{the} economy will deteriorate and trade will not expand.

These latter considerations argue against being too passive, even at the risk of giving the Indians the wrong impression. I assume we do not want to end up looking as if we are contributing, and deliberately so, to the woes of the subcontinent which seemingly must now grow even worse.



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A. ATMOSPHERICS

PRO: In general:

(a) Moves involving atmospherics are easy to make in that they entail no bureaucratic or Congressional authorization for political action or resource allocation.

(b) The Indians like atmospherics and such moves could make a broad, positive impression in India and provide a framework in which Indian policy-makers can make decisions favorable to the US on a variety of small issues as they come up.

CON: (a) Improving atmospherics could raise Indian expectations that the US is prepared to follow through on concrete political and economic issues to a greater extent than we would be willing to do.

1. Specific atmospherics: A continuing correspondence on Indo-US relations between Mrs. Gandhi and President Nixon.

PRO: (a) Provides a framework for serious high-level exchange of views on Indo-US relations.

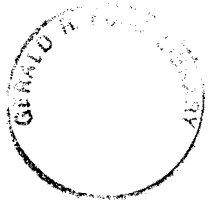
(b) Contributes to a responsible dialogue by encouraging the Indians to channel suggestions and complaints to us through official correspondence rather than through public posturing.

CON: (a) An ongoing correspondence of this sort tends to become "taken for granted" and simply a staff-level chore when there might be nothing to say; when there is nothing to say, the absence of correspondence could be taken as a negative signal.

(b) This is already being done, in substance, through Dr. Kissinger and Ambassador Kaul; and Ambassador Moynihan and P. N. Dhar -- a much better route.

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2. Following a rupee settlement, put out a statement on Indo-US relations which would amount to a sort of "principles for Indo-US relations." This could be done through either an exchange of letters between the President and Mrs. Gandhi, ^{or} a communique during a high-level US visit (perhaps by Secretary Shultz or Secretary Kissinger) timed to coincide with the signing of the settlement.

PRO: (a) Would clearly put the time of troubles behind us and provide a positive framework for future Indo-US relations.

(b) A carefully drafted document would be favorably received in India.

(c) It could offer India a balance to the Indo-Soviet treaty and publicly highlight and encourage balance in future Indian relations vis-a-vis the USSR and the US.

(d) It could have broader utility for the US in that it would highlight our readiness to establish principles for relations with the largest third-world country after we had taken such a step with respect to the Soviets, and to China in the Shanghai communique.

CON: (a) Since the Indians are the way they are, any such guidelines could provide a measuring stick for criticizing US actions with regard to India, its neighbors, or the Indian Ocean that the Indians don't like.

(b) Would unduly arouse Indian expectations.



3. Following a settlement of the PL 480 rupee question, arrange for a high-level visit to India by President Nixon, Secretary Kissinger or Treasury Secretary Shultz. (With or without option 2 above.)

PRO: (a) Could mark the end of a troubled period and the beginning of a new and better stage in our relations.

(b) Could overcome Indian feeling that the US doesn't care about India while at the same time not over-playing our interest.

(c) Could have some value for the Administration at home and highlight to American critics of past Indian policy that we have settled our 1971 disagreements and now have Indo-US relations solidly back on the tracks.

CON: (a) If our visitor doesn't have anything solid to offer, the visit might be taken as a fairly hollow gesture; if the visit didn't go off well, it could be counterproductive.

B. POLITICAL SUPPORT

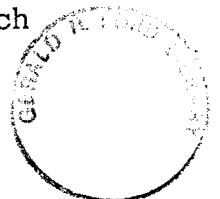
1. Offer to sell arms to India.

PRO: (a) A balance-of-payments gain.

(b) Increase our influence and contacts with the Indian military.

(c) There are some items, e.g. Skyhawks for the Indian aircraft carrier, which the Indians would like to buy from us.

CON: (a) Since we would have to sell to Pakistan as well, this would merely lead to an arms race between two very poor countries with a demonstrated hatred of each other.



(b) Advanced weapons in India's arsenal are Soviet and our action would run counter to the restraint we have urged on the Soviets in the provision of arms to the subcontinent.

(c) Indians will assume we are ending arms embargo mainly to help Pakistan, not India.

2. Offer more explicit US assurances regarding non-transfer of arms from Iran to Pakistan.

PRO: (a) Would reassure Indians on matter with which they are obsessed at little cost to us or Iran since situation in which Iran says it would transfer arms unlikely to occur.

(b) Might allow us to make political capital out of Congressional action on this issue (Magnuson Bill).

(c) There has still not been an acknowledgement to the Indian Ambassador by the Secretary or Deputy Secretary that our law prohibits such exchanges. Such an acknowledgment by one of them when the subject next comes up might help relieve Indian fears.

CON: (a) The possibility of transfers from Iran is not an openly hot issue between the US and India right now; the Indians are trying to protect themselves on this in the way we want them to, i.e., by improving relations with Iran; if we come forward with further assurances now, we may just turn the Indian search for protection back to promises by the US.

(b) We might open ourselves up to sharper backlash in the event of any Iranian arms transfers to Pakistan.

NOTE: Indian officials claim there were some transfers in 1971 and a recent INR document supports this. They ask what we have done about those. We have no reply, and this makes citing the law sound rather hollow.



3. Make a statement highlighting our recognition of India's pre-eminent position in the subcontinent and our willingness to do business with the area in terms of the 'new realities.' This might be simply an expansion and fleshing out of the President's 1973 policy statement and what you have already told the Indians.

PRO: (a) The Indians would welcome this as meeting their position on the central issue of their own foreign policy.

CON: (a) We have already said as much and gone as far as we should to meet the Indians on this.

(b) Such a statement might needlessly make India's neighbors bristle.

(c) Practice is more important than polemic here. India knows we no longer see our interest in at least one of these countries (Nepal) as derivative of our interest in India. We are not going to allow an Indian veto on our relations. We are already careful to inform the Indians in Kathmandu, Colombo and Dacca of our programs; the only additional effort we could make would be to tell the Indians more in Delhi.

(d) Indians might suspect we are trying to portray them as having expansionist, hegemonic intentions in South Asia. They already have reacted adversely to comments on India's new power status.

4. Indicate our desire for closer political cooperation and consultation on international issues and our intention to support India on issues important to India when we can.

PRO: (a) There are likely to be occasions when India wants our help on getting its nominees in international offices and in supporting Indian positions in various conferences; we can probably help on some of these issues and we can point them out as illustrative of our cooperation.



(b) Will help us obtain quids pro quo on issues where we want Indian help.

CON: (a) There will continue to be many issues and UN resolutions where the balance of our interest will lead us not to support India and vice versa.

(b) If a dramatic indication of improved Indo-US relations is wanted, this does not fill the bill.

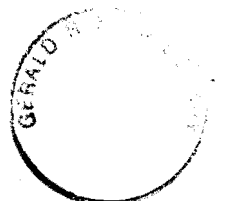
5. Promote and support a permanent Indian seat on the UN Security Council.

PRO: (a) The Indians would be flattered by such a dramatic demonstration of the significance the US attaches to the Indian voice in international and UN affairs.

(b) Such a move might marginally undercut rumblings in India that it needs the bomb to be taken seriously.

CON: (a) On balance, the Indians may not want a permanent UNSC seat at this time since it would place them on the firing line regarding international issues they would rather sidestep. They have said nothing about this recently.

(b) This move could be a disaster in light of a variety of factors relating to the dynamics of the UN, our recently enunciated support of a permanent Security Council seat for Japan, and the unpredictability of India on the Council.



6. Offer to support a more prominent Indian role in Southeast Asian affairs.

PRO: (a) This might marginally help India develop a constructive relationship with Southeast Asian countries in the post-Viet-Nam period.

(b) It might assuage Indian feelings (which are not strong) over being shut out of a voice in Southeast Asian affairs by the US (our opposition to Indian participation in the new International Control Commission for Viet-Nam); what some Indians see as US-Chinese plans to settle the future of Southeast Asia; and proposals to expand the Western-oriented Association of Southeast Asian nations.

CON: (a) Such a move would be viewed with puzzlement and suspicion by Southeast Asian countries which dislike and mistrust India.

(b) The limitations on India's capacity to participate in Southeast Asian affairs was set by its own weakness, lack of consistent interest in the area, and preoccupation with South Asia; it would be quixotic for us to take up the cudgels for India on this.

7. Make a statement indicating our recognition of the importance of India in the Indian Ocean context and our willingness to consult and cooperate with India regarding international issues and our own actions relating to this area. This statement might refer specifically to the Indian Ocean Zone of Peace proposal, question of US bases for military operation, or fleet movements in the area.

PRO: (a) This might stimulate Indian interest in accommodating the US on issues important to us in the Indian Ocean rather than confronting us head on through their posture on no bases by outside powers, etc.



CON: (a) This could complicate our ability to manage and downplay with the Indians postures that they take for domestic and "non-aligned" reasons regarding US bases and military activities in the area.

8. Tell the Indians that after the POWs are returned we will encourage the Chinese to improve relations with India.

PRO: (a) This might marginally undercut residual Indian suspicions that the US and China are conspiring against India.

CON: (a) The Chinese are going to do this anyway and the Indians know it.

(b) Because of the greater importance of our bilateral relations with the USSR and with China, we should not insert ourselves into their triangular maneuverings and suspicions.

9. Propose another round of Indo-US bilateral talks.

PRO: (a) Since these were held in 1968 and 1969 but postponed in 1971, this would be a concrete indication that 1971 has been put behind us.

(b) The talks could be as substantive as desired. (The first two rounds followed the general formula of each side stating its position on world issues. It had been proposed that the 1971 round get down to specifics of the Indo-US relationship, but they were never held.)

CON: (a) Such talks aren't much use unless they are specific, and we can handle the specifics just as well by discussions by the Ambassador here in Delhi.



(b) Maybe holding them would be too much of an indication of a return to the status quo ante.

(c) The talks in the past have more often generated heat, not light.

10. Propose reconsideration of a Treaty of Friendship, Commerce and Navigation.

PRO: (a) It would be symbolic of improved relations.

(b) The substance, which mainly concerns trade and investment, would mesh nicely with our emphasis on a new economic relationship in which aid plays a much smaller role.

(c) The GOI might be interested in the general idea of a broad agreement of friendship as a counterweight to the treaty with the Soviet Union.

CON: (a) We follow a fairly rigid format for such treaties -- a format which the Indians in the past have rejected. One point of particular difficulty concerns our provision about independent determination of compensation in the case of expropriation. This clashes with the Indian constitutional requirement that Parliament is supreme when it comes to setting compensation. Ambassador Jha raised with us the possibility of some kind of agreement about the time when India signed its treaty with the Soviet Union. He dropped it when we went over our format with him. Since then there has been the constitutional amendment re-establishing Parliamentary primacy in setting compensation.



11. Respond favorably to Ambassador Kaul's suggestion of a cultural exchange agreement.

- PRO: (a) This would ensure that at least the amount of exchange specified in the agreement takes place. Presumably this would mean an expansion of the current low level of American academic travel to India and resumption of travel to the United States by Indian politicians and journalists under the International Visitor Program. It might also help get American films and cultural presentations into India.
- (b) It would help end Indian suspicion that our programs are somehow subversive.

- CON: (a) We have such agreements mainly with communist states because these states wish to maintain extremely rigid control over exchanges.
- (b) Many of the things -- such as exchange of films and cultural presentations -- simply wouldn't work.

C. ECONOMIC COOPERATION AND ASSISTANCE

1. Take the lead in supporting the FAO proposal for establishing an emergency food stockpile, perhaps including a major storage facility for South Asia and India.

- PRO: (a) Demonstrate to the Indians that we have a sincere concern in assuring a fair share of the world's foodstuff for emergency distribution in countries like India.

- CON: (a) In order to bring off such a world food bank, the US might have to bear a disproportionate share of the financial and the material cost of the plan.

- (b) Locating the storage factory in India might make it difficult to get food out of India to meet a shortage elsewhere if India were also short on food.



2. US support for an AID/SDR link.

PRO: (a) India would view this as a major concession to its need and desire to have liquidity transferred to developing countries.

CON: (a) This reversal would be against what the Treasury Department considers to be in the best interest of the US and would undermine the role of SDR's in a reformed monetary system.

3. US Government support and guarantees for large-scale US private investment in India under terms and conditions acceptable to the GOI, probably primarily to public sector firms or in the natural resource field.

PRO: (a) Would furnish India with capital it badly needs to exploit its underdeveloped mineral resources.

(b) Letting India choose the modalities would remove fears of exploitation from foreign investment.

CON: (a) Would be difficult to interest US investors, even with OPIC or other guarantees and with Export-Import Bank financing, if the GOI determines operating conditions and repatriation rights.

(b) Would involve the USG heavily in investment matters and set a dangerous precedent for our investments elsewhere.

4. USG help to get India the American technology it desires with royalties and other costs paid by the USG.

PRO: (a) Furnishing India technology useful to it at its stage of development without strings or cost attached would be warmly welcomed.



CON: (a) Apart from the Government budgetary expense, US firms would be reluctant to part with good technology without some control over the way it is used.

(b) American trade unions might look on this as an export of jobs financed by the American tax payer.

5. A joint Indo-US economic commission.

PRO: (a) A high-level joint economic commission would please India by demonstrating genuine US interest in India.

(b) Provide a forum for discussion of bilateral problems and opportunities.

CON: (a) The Indians might use this as a vehicle for floating unacceptable bilateral and other initiatives.

(b) Would lead to pressures for similar joint economic commissions with other countries, e.g. Pakistan.

(c) Unless the joint economic commission actually accomplished something, it could be counterproductive.

6. Support India's aspiration in international trade and tariff.

PRO: (a) Many US and Indian objectives in the international trade front are similar, e.g., our mutual opposition to reverse preference arrangements.

(b) Giving India and other LDC's better access to US and other industrial countries' markets would be warmly welcomed by India.

CON: (a) India might press for an annual trade plan (a la rupee bloc) and this would be unacceptable to us.



7. Offer Mrs. Gandhi a major and special joint US-India program to make India self-sufficient in agricultural production. Such a program might include: provision of fertilizer; investment in new fertilizer plants; investment in new power plants for rural electrification; help for tube wells and other irrigation facilities; research on new seeds, etc. The US could provide a maximum of financing and minimum of technical assistance (no intrusiveness).

PRO: (a) This is a limited, desirable field of economic assistance in which we could make an impact.

(b) Would be popular both in India and at home.

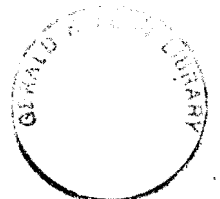
CON: (a) Without a proper atmosphere it could lead us into the same sort of misunderstandings that have characterized Indo-American relations in the past.

8. Propose a double-taxation agreement.

PRO: (a) This would simplify life for American businessmen, journalists, etc., living in India and would, as a result, encourage trade and investment. (GOI "Indianization" requirements would presumably continue.) It would also probably simplify things for the estimated 300,000 Indian nationals in the US.

(b) We just signed such an agreement with the Soviet Union. This might both reduce Indian opposition and increase the symbolic value.

CON: (a) There isn't much in it for an India which doesn't want imports or investment from the U.S. and which isn't interested in a large American presence in India.



9. A substantial one time grant of fertilizer.

PRO: (a) This would give the Indians almost immediate help in an area in which they need it badly. They have a fertilizer purchasing mission in the US now.

(b) This offer would emphasize Indian self-sufficiency, i.e., grow it here.

CON: (a) Fertilizer is in very short supply in the US and would be hard to find.

(b) This would be aid before the Indians had asked or established the proper atmosphere.

10. An immediate and substantial (\$75 million) development loan for commodity assistance to India.

PRO: (a) This is help where the Indians need it most (balance of payments) and when the Indians need it most.

(b) This will be the least intrusive form of aid; the Indians would have the maximum flexibility in regard to using it.

CON: (a) This would get us back to the old style of aid and US-India relations and overturn our present strategy.

(b) This would also return us to a type of assistance the economic effectiveness of which is very doubtful.





DEPARTMENT OF STATE

Washington, D.C. 20520

January 8, 1974

CONFIDENTIAL

TO: NEA - Joseph J. Sisco
FROM: NEA/INS - L. Bruce Laingen
SUBJECT: India - What's Next? -- Information Memorandum

Now that we are successfully settling the rupee problem, we need to examine how we maintain the momentum in shaping a more mature and steady relationship with India. This paper reviews where we are and where we seem to be heading.

Political Relations

-- Politically, we are in relatively good shape. For the moment, at least, we see no clash over our respective South Asia policies or on third country issues. In talks with the press in Delhi, Tikki Kaul is stressing the positive. The only bilateral cloud, as yet a potential problem, concerns likely Indian opposition to any large-scale expansion of US naval presence in the Indian Ocean.

-- Simply maintaining the dialogue begun in 1973 should help consolidate the improvement in relations, without stirring unrealistic expectations. A visit by Secretary Kissinger in 1974, of which he talked with Ambassador Kaul, would give a further fillup, symbolically underscoring our success in putting 1971 behind us and moving toward a new basis for Indo-US relations.

Economic Relations

-- The agenda lacks spectaculars to follow the rupee settlement, but there are sufficient possibilities to afford a reasonable chance of showing progress toward a new framework for our relations, which the President proposed in the 1972 Foreign Policy Report. The energy crisis adds new importance to the economic relationship. Because of heavy dependence on imported oil, India's foreign exchange position is badly threatened by recent price hikes which the GOI fears will cost \$500 million

CONFIDENTIAL GDS

lba 1/10/07



annually, wiping out Indian reserves in two years.

a. Economic Assistance: Given India's continuing economic malaise - and now the energy crisis - the GOI is likely to approach us in Delhi regarding possible new bilateral aid. Before we offer any, we and the Indians should agree on the form and acknowledged common purpose of aid; we also want clear understanding that the GOI will not resume irresponsible public criticism of US assistance. In terms of amounts, AID now concedes that it can probably find \$15-20 million for a late FY 74 loan if needed. For FY 75, OMB has slashed the State/AID recommendation of \$150 million in half.

-- Whatever happens in the aid talks, we see bilateral assistance as playing a much reduced role in our economic relationship with India, with the bulk of US support for Indian development coming through multi-lateral channels, through IDA.

b. Trade and Investment: We and the Indians have stated we want to stress trade rather than aid. Accordingly, we expect they will also respond to our proposal for talks in Delhi on trade and investment questions.

-- We have no fixed agenda for these talks, but think they should focus on means to increase US exports to India and Indian exports to the US rather than vague principles and hopes.

-- Our analysis suggests only limited potential for trade expansion. (Two-way trade has run about \$600 million annually, not including aid. We are India's largest trading partner; India is 26th for us.) Nor are current prospects for large-scale US investment bright, although a number of companies are bidding for offshore oil sites and the Indians are moving toward a more pragmatic approach on foreign investment.

-- Still, bilateral trade promotion efforts could yield some results. We are seeking to provide a sharper focus for the normal flow of economic visits, e.g. upcoming Commerce Department trade missions, Department of the Interior research team, etc.



Prospects
for real
results
not so
hot.

-- Embassy Delhi has suggested negotiation of tax and friendship, commerce and navigation treaties. We are currently exploring these possibilities.

-- We expect the Indians may suggest some form of joint economic committee. This might be useful if it focuses on practical problems and does not invite illusory hopes. (See below for fuller discussion of Joint Commission concept.)

c. Science and Technology: A working-level review among concerned agencies has concluded that a modest USG effort to promote S & T exchanges, cooperative ventures and research with India would be worthwhile. The emphasis should rest on cooperation and mutuality rather than technical assistance. Embassy Delhi shares this view.

-- A private group of senior US and Indian scientists is meeting January 9-12 in India under Pugwash auspices. The session is likely to produce recommendations on enhancing cooperation.

-- The Indians have approved a resumption of joint agricultural research projects funded with US owned rupees. We now expect them to follow suit in other areas of joint research. They may also propose an Indo-US S & T agreement. We have concluded a number of these in recent years and would have no objection to one with India, as long as it promotes, rather than restricts S & T interchange.

d. Education and Culture: The easing last fall of Indian restrictions on US scholars has mitigated a major complaint of US academics. Top US and Indian educators are meeting in Delhi this week and presumably will recommend ways to enhance educational interchange.

-- The Indians have spoken of a possible cultural agreement. We have made clear our lack of interest in such an arrangement, which CU would strongly oppose.

Joint Indo-US Commission

-- Last month during his pre-consultation round of calls, Tikki Kaul talked of setting up an Indo-US commission once the rupee problem was solved.



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-4-

The idea of some sort of economic Commission originally came up about a year ago in a conversation between Dr. Kissinger, Ambassador Jha and Finance Minister Chavan.

-- The concept remains vague. We have a variety of extended joint arrangements with the Japanese, Canadians, and Soviets. We, of course, have binational education bodies with many countries. In recent years we have also set up joint S & T groups with Poland, Israel, France, and Yugoslavia, in addition to Japan and the Soviet Union.

-- We think we should keep an open mind on this. We will want to hear what the Indians finally suggest. In the meantime, we will get a better fix on how such arrangements have proven with other countries. Conceivably something useful could develop. In case the Secretary goes to India, this might be a logical product of his visit.

Deputy Secretary Level Consultations

-- The Indians have not recently talked with us about reviving Deputy Secretary level consultations which were held in 1968-69. Our relations are now at a stage where this is possible. However, we wonder about the desirability. The consultations proved not very productive, and we prefer to explore new approaches such as the joint commission idea.

Du
Drafted:NEA/INS:DKux:mmk 1/8/74
Concurrence:NEA:SSoer

~~CONFIDENTIAL~~



THE WHITE HOUSE
WASHINGTON

80

John

Let's work on Hal.

Say I sent memo in he
approved - but my own
views are more negative
& elaborate.

Z



MEMORANDUM

NATIONAL SECURITY COUNCIL

CONFIDENTIAL (GDS)

February 13, 1974

Handwritten: E 3b
INDIA

MEMORANDUM FOR: CHUCK COOPER
FROM: HAL SAUNDERS *for*
SUBJECT: Aid for India

I would recommend that your memo be modified to the following extent: Instead of suggesting that Ambassador Moynihan in effect rebuff India's expressed desire for aid talks, the memo could suggest that India be told (a) that we don't want aid talks to get too far ahead of the important talks we and they envisage on trade/investment, and (b) that we therefore would prefer to start aid talks at about the same time both sides are about ready to start trade/investment discussions. This is not all that different from the recommendation in your memo; it is basically just a way of taking a slightly less negative tone with the Indians.

Alternatively, you could add the following paragraph^s to your memo:

"Hal Saunders feels it would be damaging to our relations with India simply to refuse to enter into aid discussions with them at this point. He argues that the Indians have requested such discussions in response to our aide-memoire of last summer, and that it would therefore be a sharp rebuff to them if we were to shift our position and refuse now to start such talks. The Indians are already edgy over our Diego Garcia expansion plans, and a US refusal now even to start talking about possible aid could foster a stepped-up Indian campaign against our Indian Ocean policies. Hal acknowledges that it is hard to see a significant US aid program in India given our resources. However, at this point it may be better to reach that view together rather than refuse to talk about the subject. He points out that both we and the Indians realize that any US aid is likely to be little more than symbolic; that they agree that aid is to be a small and subordinate part of an overall US-Indian economic relationship that focuses primarily on trade and investment; that they appear to want some US aid, even a small amount, as a way of demonstrating at least some semblance of balance in their relationships with the two super-powers; and that an aid dialogue with them could begin soon even if there is no money available for 1974.

CONFIDENTIAL (GDS)

Handwritten: 1/10/07



MEMORANDUM



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10

NATIONAL SECURITY COUNCIL

ACTION

~~CONFIDENTIAL~~

February 13, 1974

K

MEMORANDUM FOR: SECRETARY KISSINGER
 FROM: CHARLES A. COOPER
 SUBJECT: AID Assistance for India

*Agree follow
off track?*

With Ambassador Moynihan in town State/AID is trying to get your approval for initiating our AID program in India during FY-74 or at least in FY-75. With the Congressional cuts and diversion of AID funds to Vietnam, there is virtually no room in the FY-74 program for India. Should we scrape up a minimum amount, say \$10 million, such assistance would be insignificant in the India situation but might initiate an expensive and controversial arrangement for the future. The increase in petroleum prices costs the Indians about a billion dollars a year, so any assistance we might provide is economically insignificant.

The key issue is the order of our dialogue with the Indians. We had originally envisaged a three-part dialogue--first the rupees, then trade/investment and aid, with any aid relationship seen as clearly subordinate to the role of trade and investment. Now, however, Moynihan and the Indians are proposing that we move ahead on aid discussions in advance of talks on the trade relationship and investment climate.

There are two good reasons not to let aid talks get substantially ahead of the more important talks we envisage on trade and investment:

-- We do not have funds for a major aid program and will find it hard to get Congressional support. Prior movement on the investment and trade climate would help increase Congressional support for AID appropriations.

-- The Indians create many of their own economic problems by over-regulation, state ownership and restrictions on their private sector. AID assistance will make only a small difference in the Indian economy; changes in Indian policies on investment and trade could make a major difference and private investment and trade flows from the U.S. combined with aid might make a real difference.

The reasons for not responding in a completely negative way to India's request for aid talks are political, not economic. The Indian request

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for such talks is in response to Moynihan's aide-memoire of last summer, and a sudden U.S. shift now to a totally negative stance would be seen as a sharp rebuff. It would be taken by the Indians as a negative signal and might foster greater Indian criticism of U.S. policies such as our current Indian Ocean activities.

RECOMMENDATION:

That you suggest Ambassador Moynihan respond to the Indian request for aid talks by telling them:

-- Since both countries envision expanded trade and investment as the centerpiece of our future economic relationship, we think aid talks should not get too far out in front of trade/investment discussions.

-- We would prefer to start aid discussions about the same time both sides are ready to get trade/investment talks started.

Hal Saunders concurs.

KS



— 2/20/74 10a

NATIONAL SECURITY COUNCIL

John Bushnell

For your info,
attached is a
copy of State's
memo to HAK on
aid to India, which
I just received.
- Hank A.





DEPARTMENT OF STATE
ACTION MEMORANDUM

S/S

FEB 12 1974

AID-1 740324S
~~J. Sisco~~
2 Bushnell 10b
Probably not too bad

CONFIDENTIAL

To: The Secretary

From: NEA - Joseph J. Sisco *JJS*

Not too good return.

Aid to India

CC

We need your guidance to respond to an Indian request to begin discussions on the future of our bilateral economic aid relationship.

* * *

In June 1973, the President authorized discussions with India to see if agreement could be reached on the form and purpose of bilateral assistance. In July, Ambassador Moynihan informed the Indians of our willingness to begin such discussions. Both we and the Indians, however, were in tacit agreement that it would be premature to begin such discussions until negotiations on the rupee agreement were concluded.

We have made clear to the Indians that we do not see such discussions leading to a massive and highly visible donor-client relationship of the kind we had before with India. We have emphasized that we hope to see trade and investment become more the focus of our relationship. Finally, we have stressed that before there can be a resumption of bilateral aid, such aid must fit within the context of a satisfactory total relationship in which it was clear that India wanted our aid and said so.

Since 1971 we have provided no new bilateral aid to India other than annual debt rescheduling (\$29 million) and a PL-480 Title II program (\$35 million in FY 74).

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GDS - Declass 2/11/81

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We believe the atmosphere is now good for aid discussion. We expect to sign the rupee agreement on February 18. ~~The Indian leadership has generally stopped publicly attacking us.~~ India appears receptive to international cooperation in dealing with the energy crisis. The Indian Government looks forward to ~~your own visit to Delhi this spring as an opportunity publicly to emphasize the new maturity in our relations.~~

bully

We therefore believe we should respond favorably to the Indian request for talks on aid. The problem, however, is money.

Ambassador Moynihan cannot enter into such discussion in good faith without the assurance of funds being available should the talks proceed well. The \$75 million earmarked for India in FY 74 has now virtually disappeared, because of the demands from other areas. A similar amount tentatively proposed for India in FY 75 is obviously far from certain at this point in time.

Options

We see three possible lines of approach: First, we could respond to the Indians that aid resources are so limited that all our future aid to India must be in the multilateral channel. Second, we could tell the Indians that no funds are available for FY 74 but that we would be prepared now to begin talks leading to possible aid in FY 75 within a planning figure of \$75 million, subject, of course, to final availability of funds. Third, we could seek to locate a small amount, say \$15 million, from FY 74 funds, telling the Indians that we would be prepared to begin talks now, possibly leading to a first and small amount of aid this fiscal year but with no assurance of any funds before FY 75.

1. No Assistance. Following this route would be attractive in terms of the severe demands on available funds for the future. However, we believe it would not be appropriate for our future relations with as large a



~~CONFIDENTIAL~~

-3-

developing country as India and would be inconsistent with the position we have taken with the Indians over the past year that we would be prepared to talk about future bilateral aid in the context of an improved overall relationship.

2. No Assistance this Fiscal Year. It does not appear feasible under the best of circumstances to allocate any substantial sum for development lending in FY 74. Moreover, it may not be possible, in practical terms, to reach agreement with the Indians on the mechanics of future aid in the few months remaining in FY 74. We could, nonetheless, begin discussions now. We could point out that while we cannot hold out the prospect of aid in this fiscal year, we think we could usefully begin talking now about a possible understanding for aid in FY 75, within a planning total of \$75 million, subject to final Congressional action and availability funds. We would proceed on the assumption that no aid funds would be available for FY 74, but that should a small amount nonetheless later become available, we would consider using it for India, depending of course on the progress of our talks there.

3. Begin Aid this Year; but with Principal Focus on FY 75. The Indians have now made it fairly clear that they want us to resume bilateral aid and apparently will be receptive to our views on the kind of public framework in which this takes place. Therefore, we believe that talks could lead fairly promptly to a specific and tangible aid request. Our responding promptly with even a small amount of aid, say \$15 million, within the next few months would help ensure continued momentum in improved US-Indian relations. It would also provide a good base from which to continue more detailed discussions of a somewhat larger but still relatively modest aid program in FY 75. A.I.D. indicates, however, that a firm commitment of as much as \$15 million for FY 74 cannot be given at this time without disruption of other established and critical priority programs. They report that this situation might be even worse if Congressional action on the pending disaster relief authorization is partly or wholly negative.

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Recommendations

1. We and AID recommend Option 2 above, i.e., that you authorize us to inform the Indians that, given limited aid funds for FY 74, we would be prepared to begin discussions on the form and purpose of possible assistance only for FY 75, within a planning level of \$75 million, subject to appropriations and loan availabilities. We would also say that if, by chance, there might be some small amount available (say, \$15 million) near the end of the present fiscal year, we would see what could be done.

NO

Approve _____

Disapprove _____

2. Alternatively (should you conclude that we need to be in a firm position to begin aid to India this fiscal year) you could direct that \$15 million of FY 74 funds be earmarked for India and that we be authorized to begin discussions now with the Indians on the form and purpose of assistance up to the \$15 million level in FY 74, continuing in FY 75 at a planning level of \$75 million, subject to appropriations and loan availabilities (Option 3). As indicated above, AID believes that fund availabilities preclude this option.

Approve _____

Disapprove _____

Drafted: NEA/INS:DWBorn:hme/gmd
x20701 2/14/74

Concurrences: NEA/INS-Mr. Laingen
NEA-Mr. Sober
AID/ASIA/SA-Mr. White



11a

UNITED STATES GOVERNMENT

Memorandum

TO : See Distribution Below

FROM : ASIA/SA/SIN, Alfred W. Ford
Room 6732 NS

SUBJECT: India Consortium

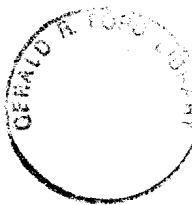
DATE: May 31, 1974

Pursuant to Mr. Mosher's memo of May 24, attached are background and discussion papers prepared for the Inter-Agency review scheduled for June 5. These papers were prepared hurriedly due to last minute arrival of key Bank documents. Under the circumstances, it would be helpful in developing the final U.S. position at the June meeting, if the various U.S. agencies would provide the inter-agency meeting with written expressions of their views on specific issues.

Attachments: a/s

Distribution:

Treasury, Mr. Pelikan
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Commerce, Mr. O'Rourke
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AA/PPC, Mr. Shakow
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ASIA/SA, Mr. Rees
ASIA/SA, Mr. Coles
ASIA/SA, Mr. Ford
NEA/INS, Mr. Born
AA/PPC, Mr. Birnbaum



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PAPERS FOR INDIA INTER-AGENCY REVIEW

A. The Economic Situation

1. Bank's Findings (TAB A)
2. A.I.D. Assessment (TAB B)

B. Issues for the U.S.

1. Effect of Nuclear Explosion on our plans for aid (TAB C)
2. Debt Relief (TAB D)
3. GOI performance (TAB E)
4. Food (TAB F)

C. Consortium Meeting, Paris, June 13, 14

1. Historical background (TAB G)
2. U.S. Aid Statement for June 1974 meeting (TAB H)





SUMMARY AND CONCLUSIONS

i. These are times of unusual difficulty for the Indian economy. The Fourth Plan period has just ended with large shortfalls in most of the Plan objectives and with average economic growth for the period of about 3.5% a year (in line with the twenty year trend) instead of the 5.7% at which the Plan aimed. Most of the growth was lost in per capita terms to the steady expansion of population which went on at about 2.3% a year. The latter part of the Plan period was a time of increasing shortages of food and other essentials and of mounting inflation, with only favorable exports and the maintenance of satisfactory foreign exchange reserves to add a bright spot to the economic scene. Then in recent months, the external impact of oil prices and other changes for the worse in India's terms of trade have compounded the difficulties of the current economic situation.

ii. It is in these adverse circumstances that India has had the unenviable task of preparing its Fifth Five Year Plan for the period April 1974-March 1979. The Plan is now in draft form which, in contrast to the disappointing results of the Fourth Plan, charts a buoyant course for the Indian economy over the next five years. It sets an economic growth rate of 5.5% with major improvement in both agricultural and industrial production and with changes in income distribution to the relative advantage of the large numbers in the lower third of the income scale. It is not at all clear, however, how the economy is to move from the disappointing experiences of the Fourth Plan onto this buoyant course. Nor in the aftermath of recent economic misfortunes does it seem possible. The Draft Fifth Plan is therefore to undergo revision which presumably will take account of needs for adjustment to current difficulties over the next year or so with minimum adverse economic consequences, as well as needs for as much longer term economic progress as is realistically possible in spite of current difficulties.

iii. This report has a similar divided emphasis on both short-term problems and how they might be managed, and on the longer term problems and potentialities of India's economic situation. The latter are considered from the broad standpoint of prevailing circumstances and possibilities for advancement in the various sectors, rather than from the standpoint of particular target probabilities. In view of the currently uncertain basis for quantitative economic projection and of the prospective revision of the Fifth Plan Draft, the report does not attempt any systematic consideration of macroeconomic parameters.

Short Term Adjustments

iv. For the short term there is a range of adjustments to be faced which arise out of the shortage of domestic supplies and services, high costs and scarcities of imports, and the consequent inflationary and balance of payments difficulties. Inflation is being confronted on the fiscal and monetary front, but with uncertain outcome in view of continuing price pressures related to rising current expenditures and physical shortage especially of food and other wage goods. The problems of balance of payments adjustment are deferred for discussion below,

except to note here the austere levels of imports of oil, food and other maintenance materials that are implied.

v. The important short-run supply and allocation problems to be dealt with in this context of shortages are how to curb oil consumption with minimum adverse effects on agriculture, industry and transport; how to raise and transport more coal for which an improvement in railway labor relations seems imperative; how to get more out of existing power, fertilizer and steel capacity while moving ahead with additional capacity; how to ensure delivery to agriculture according to agricultural priorities of as much of its needed inputs as can possibly be made available; how agricultural surpluses and food imports can be most effectively distributed with special consideration for the needs of the poor; and how within the limits of present constraints to get a better performance out of industry.

vi. This is a large order. It suggests the need for focus of economic management on a few particular problems of production and distribution, while allowing greater freedom for decentralized decision and operation with adequate price and other incentives both public and private enterprise. Current trends of policy appear to be in these directions. For central economic management, perhaps the most difficult demands are those of assigning limited foreign exchange among competing import claimants, of improvement needed in the systems of priority allocation and delivery of essential supplies (oil, coal, fertilizer, steel, power, food), and of the need for satisfactory labor relations in essential operations and especially in railways and power. With incentives and arrangements for efficient use of available supplies and capacities it should be possible to start some revival of production which in company with fiscal and monetary restraint is the best hope for curbing inflation.

The Broader Development Issues

vii. Beyond the imperatives of short term economic planning and management, India continues to face as difficult a range of chronic development problems as are probably to be found in the developing world. Development strategy must therefore have a broad focus - ever larger food and other agricultural production, more rapid industrial growth in which special emphasis is placed on what are known as core sectors 1/, maintenance of adequate economic services especially transport and power, and improvement of the quality of human resources through social services such as family planning, public health and education, and by upgrading the employment, productivity and incomes of the poor.

Human Resource Improvement

viii. The state of human resource problems and programs may be mentioned first. There is hardly need to emphasize the crucial issue of population growth

1/ The industries singled out for special mention and provision in the Budget Message for 1974/75 are coal, steel, non-ferrous metals, fertilizer and power.



in India's longer term prospects. The rate of growth is not so unusually high but it is the enormous size of the population, now nearing 600 million, and the annual increments at about 13 million which are so overwhelming. India has the oldest and largest public program of family planning with substantial achievement to its credit but with a recent record which is disappointing in relation to the seriousness of the problem. The estimated proportion of couples of child bearing age now practicing family planning is 15% which, while representing very large numbers, is well below the ambitions of the Fourth Plans. So also is the decline in the birth rate, now about 35 per thousand of the population, a creditable drop from the 39 per thousand in 1968, but still higher than last year's objective of 32. Most of the contraception programs have tended to lose momentum; first the use of the intra-uterine device, and more recently the vasectomy program after large successes during 1972/73 on the basis of mass vasectomy camps with attractive incentives. The legalization of abortion marks an important advance of recent times in means of population control. As yet it has not played a significant role in the family planning program, although potentially its impact could be substantial. The part of the program in which there has been sustained success has been promotion of the use of condoms.

ix. Reasons for the disappointing recent results probably reflect both social and economic reasons for lack of family planning motivation and shortcomings of the program itself. Program revisions are now proposed in the course of further expansion and closer integration with an expanded public health service in an effort to overcome past shortcomings, develop a better understanding of the nature of family planning motivations, and further increase the numbers of couples practicing contraception to 40-42 million in 1978 from the present estimated 28 million while reducing the birth rate to 30 per thousand. It is difficult to assess prospects for achievement of these objectives in the absence of a better understanding of motivations and with all the uncertainties of the program, especially because of the tight budgeting prospects.

x. Education is another area of important social development with considerable achievements over the years in numbers of schools and students and improvements in literacy but with manifold and seemingly intractable problems to be faced. These problems are associated with the vastness and diversity of the population to be educated, the severe shortage of funds in relation thereto, the strong pressures and interests in education, and lack of clarity about educational aims and priorities. The consequences of all this has been an excessive bias under strong political pressures for higher education with insufficient provision for elementary education. Graduates at the secondary and university levels have exceeded employment opportunities at their qualification level, while at the same time the elementary levels have been characterized by inadequate facilities, poor standards and high wastage. Educational aims are for a very large expansion over the next five years with a shift in emphasis as compared with the last five in favor of elementary levels. This will be in further pursuit of the constitutional obligation to provide universal elementary schooling. Again, however, achievement may be hampered by shortages of funds (education has fared poorly in relation to its program in the 1974/75 budget), continued rising demands for higher education, and uncertain educational directions.





xi. Perhaps the most basic of human problems in India is the vast extent of poverty-unemployment-underemployment. It is difficult to separate these concepts along Western lines in circumstances where there is the tendency for the work force to adapt to the work available on the basis of casual, low productivity, low income employment. The Fifth Plan lays particular emphasis on the impoverished state of perhaps half the Indian population and the need for relative improvement of this part of the population in any acceptable notion of development. But this conception of development is not novel with the Fifth Plan. The importance of the distributive as well as the productive aspects of development have been explicit throughout Indian development policy since the First Plan in 1951/52. Doing something about it has been another matter especially because of the size of the problem in relation to resources and because of the difficulty of the basic solution to the problem - improvement of productivity among the poor.

xii. Large programs aimed directly at raising the economic state of the poor were undertaken in the Fourth Plan period with limited success. They did however provide extensive experience in the nature of the difficulties to be surmounted. Continuation of these efforts with modification in the light of Fourth Plan experience is contemplated in the next five years. These are to be supplemented by increased attention to the poorer population in the provision of economic and social amenities ("minimum needs"). Problems remain formidable nevertheless because of the likelihood of resource constraints, technological limitations especially in the drier rural areas, and strong institutional and administrative obstacles to be surmounted.

Agriculture

xiii. As always, these human problems and the general health of the Indian economy rest to a great extent on the fortunes of agriculture which in turn still depends very much on the weather. The marked extension of irrigation and the dramatic improvement in the technology of mainly wheat cultivation in the past few years (the "green revolution"), have made Indian agriculture somewhat more reliable in recent years. Yet the limited influence of these changes on the vast expanse of Indian agriculture as a whole is indicated by the wide variations in foodgrain production during the last five years from a peak of 108 million tons in 1970/71 to 95 million tons in 1972/73, a year of severe drought. In spite of these fluctuations agriculture has maintained a long-term trend of about 3.5% increase per year. There are however reasons for concern that some adverse shift in the trend may be taking place in recent years possibly because of lags and interruptions in the application of the new technologies to wheat and delays in the development of improved technologies for rice and other crops. Part of the problem of recent times has been shortages of essential inputs like fertilizer, improved seed and power for irrigation and mechanization. This year after a very favorable autumn harvest, the harvest currently in progress is below expectations for the reasons indicated above and unusually low winter rains.

xiv. The effects of slow growing and variable agriculture has been the major influence on the recent course of national income. This is because industry which should be pacing the growth of the economy has been in the doldrums with only minor spurts since the middle sixties. In recent times it

has only been in the favorable agricultural period of 1967/68-1970/71 that there was satisfactory growth in real national income at average rates of between 5% and 6%. There was little further growth in the next two years as agricultural production fell because of poor harvests and industry continued on its slow course. There was again a pick-up last year reflecting again the favorable harvest of last autumn.

xv. In these times of low world food stocks and surpluses it is imperative for India to improve its food security. Almost as important is a rise in the stagnant trend of cash crops. These are interrelated problems. Both depend on the creation of additional acreage through irrigation and double cropping (there is little remaining unused land suitable for cultivation) and on improved yields. The potential for the latter seems larger in the food crops than the cash crops. Hence the key to satisfactory and balanced agricultural development is the larger irrigated acreage (with related land improvement measures) and a very substantial advance in grain yields. Such yield improvements would allow for the use of a large part of the additional gross acreage for cash crops. This whole pattern of performance will depend on both a better record of agricultural improvement and better luck on the weather during the next five years than in the last five.

xvi. The problem of the last five years has not been that the "green revolution" was overrated. In fact the spread of the new varieties and methods and their contribution to production and to the public distribution system has been dramatic indeed. But recent progress has suffered from the delayed, although soon expected, technological breakthrough in crops other than wheat; by deterioration, and slow development of replacement varieties of high yielding seed; and by shortages of fertilizer and power for irrigation without which the "green revolution" has little meaning. Fertilizer, power and seed supplies will probably continue to be problems for the next few years but it should be possible to minimize their constraint on agricultural development through feasible improvements in systems of production and delivery of these essential supplies. With this, and if the expected technological advances in rice and other crops really materializes (and of course if the weather is helpful) it should be possible in the next five years to improve considerably on the agricultural record of the last five.

xvii. Along with the problems of agricultural production there are the additional difficult questions of how to distribute food so that a share is available for the lower income groups at prices they can afford, and how to increase the productivity and income of small and poorly located farmers.

xviii. Food supply at "fair prices" is handled through a public procurement and distribution system. As would be expected, the system works best when it is least needed, i.e. when supplies are plentiful, prices are steady, speculation is low and procurement is easy. It works worst when it is most needed for the reverse reasons. In the past two years of shortage it has not worked well - public procurement has been far below targets at a time when demand on the public distribution system has been unusually high. The attempted remedy of early 1973 in which the Government took over the wholesale trade in wheat in an effort to increase procurement and reduce speculation proved ineffective. Trade in the harvests of late 1973 and early



1974 has been restored to private wholesalers whose price incentives have been substantially raised but whose obligations for delivery to official channels and penalties to do so have been greatly increased. The test of these new arrangements will come during the current wheat harvest, but it will be a difficult test period in view of disappointing harvest prospects with consequent tight grain markets, rising prices and speculative pressures.

xix. Special programs to assist the poorer sections of the rural community have concentrated on the small and marginal farmers, on employment programs to help the landless, and improvements in the environment and technology of cultivation in areas of low and unreliable rainfall. Through these programs valuable experience has been gained in a particularly difficult but important area of development. There are various indications that numbers of the intended beneficiaries of these programs have been helped. Nevertheless progress has been slower than expected and the formidable nature of the institutional, organizational and administrative difficulties has been manifest. With the experience gained, the Draft Fifth Plan proposes a large expansion in programs for the smaller and less advantaged farmers and farm laborers in the next five years. The need for much stronger infrastructure support for these programs is recognized. And it is also recommended in the Draft that land reform be incorporated as a major contribution to small farmer improvements. So far the role of land reform in agrarian advancement has been virtually neglected.

Industry

xx. Industrial production has not been of sustained help in India's need for more rapid development since the mid-sixties. It continued in this slack pattern during the last five years with an average annual growth at only about half the 8% target of the Fourth Plan.

xxi. This has been characteristic of both public and private manufacturing activity which makes up the mixed industrial sector. The absence of industrial drive since the late fifties and early sixties has numerous explanations which vary in their importance depending on different periods of time or as they apply to public or private enterprises. Two persistent industrial constraints for both public and private industry have been shortages of domestic resources, especially as they limit public investment and therefore industrial demand, and shortages of foreign exchange as they limit industrial supply requirements and in consequence adversely affect industrial incentives. The poverty and slow pace of the Indian economy is another adverse element in the broad industrial demand picture, especially in more recent times as scope for import substitution has declined in relation to the size of the industrial sector, and especially for private industry as much of the available import substitution opportunities have been preempted by the public sector. The field of export demand has not been aggressively pursued by either the public or private sector, with a few exceptions, partly because the highly protected domestic market has not been conducive to competitive capabilities in world markets and partly because of shortcomings of export promotion policy and administration. In more recent times both wings of industry have suffered from shortages of supplies and services, especially steel and power, as well as agricultural



raw materials in times of poor harvest. Inflation has also been an adverse factor in a context of rising costs and lagging price ceilings and in its unsettling effects on labor relations. All of these of course are detrimental to investment incentives.

xxii. In the public sector, capacity utilization has been low, especially in steel, fertilizer, non-ferrous metals and heavy engineering, and the construction and expansion of capacity has often been excessively slow. The Fifth Plan blames these inefficiencies not only on supply and labor problems but also on shortcomings of design, operation, maintenance and management plus a number of deficiencies of central industrial administration.

xxiii. Private industry has its own set of inhibiting influence in addition to the general problems of slack demand, foreign exchange restrictions, material shortages and labor problems. These stem from the multiple and at times incompatible objectives of national industrial policy, operating through what has become a cumbersome industrial licensing system. The objective of preventing monopoly and concentration of economic power has undoubtedly hampered individual expansion through licensing restrictions since 1969 on larger scale industry.

xxiv. More recently there has been clarification of the areas open to larger scale industrial expansion which has reduced previous uncertainties affecting private investment, and other changes have been taking place toward expeditious administration of the licensing system and easing of price ceilings. The Government is also attempting to identify bottlenecks in the operations of public sector enterprise and to improve their performance through better and more responsible management. In both the public and private sectors these moves of Government and Government policy should be helpful in the difficult circumstances of current supply shortages.

Fertilizer and Steel

xxv. Both fertilizer and steel are essential products for which there is a large domestic market and which India should be able to produce at competitive prices. Both industries have occupied a prominent place in India's development effort and have absorbed a considerable proportion of investment resources particularly of the public sector (an estimated 45% of public sector (industrial) investment during the Fourth Plan). In both cases the production record has been disappointing in relation to efforts made - particularly so in the case of steel where despite continuing investments production has actually declined during the Fourth Plan. As a consequence fertilizer and steel imports continue to absorb a significant proportion of India's scarce foreign exchange.

xxvi. The creation of new capacity in both industries once again occupies a prominent place in the Draft Fifth Plan. A major expansion of capacity is already under construction. In both cases, the number of new schemes contemplated, if phased as proposed, will represent a considerable challenge in terms of limited investment resources and capabilities to execute and manage.



xxvii. In the case of steel, the main development emphasis is on efficient use of present capacity plus that under construction. This, if successful, should satisfy domestic requirements for quite some time to come, and even allow for an exportable surplus. Some additional output from new construction is also expected late in the Fifth Plan period, but most of the output from new Fifth Plan projects is not expected until the Sixth Plan period. The creation of new capacity will not therefore provide a way out of the current production problems faced by existing units - inadequate coal and power supplies and labor difficulties. These will have to be resolved by the existing units if near-term production targets are to be reached. In the long run, however, provided efficiency can be achieved, there is no reason why India with her large resources of iron ore and coking coal in close proximity to each other should not become a major exporter of steel. Nevertheless, difficult resource issues will have to be faced in the medium term before irrevocable commitments are made to long gestation projects with heavy future financing requirements.

xxviii. In the case of fertilizers, despite the considerable capacity in existence and under construction, there is a definite need for additional capacity. Therefore, in order to maximize production in the short-term it would seem appropriate during the first two years of the Fifth Plan to start construction of an additional 2 million tons of nitrogenous capacity which is at advanced stages of consideration and can be brought into production relatively quickly. Despite the increase of world petroleum prices it is reasonable to proceed with these projects with fuel oil as feedstock both because of limitations of domestic coal supplies and because an attempt to change the feedstock at this stage would lead to delays. Beyond this, consideration of new investment decisions may have to remain flexible for the time being; though, of course, the assessment of new investment opportunities and the preparation of a shelf of projects would have to continue in order to lay the foundation of a properly phased long-term investment program.

xxix. Such flexibility, even if it should involve some delay in investment decisions, need not entail much production foregone, particularly as it would improve the chances of making better use of existing and on-going projects by enabling officials to focus on the needs and problems of these projects. Similarly, the risk would be avoided of starting projects which are slow in execution due to managerial constraints in the public sector, and which may not be fully utilized due to other constraints such as the shortages of equipment, power, coal and crude oil. By the third year of the Fifth Plan (1976/77), it should be feasible to contemplate new investments in coal-based plants in India, though firstly the possibility of joint ventures based on natural gas in the Gulf area and in Bangladesh needs to be thoroughly explored. By then the worldwide fertilizer investment picture would also have clarified somewhat and India's investment decisions could take these developments into account.

Energy

xxx. The relative importance of commercial fuels as sources of energy (measured in coal replacement terms) has grown considerably from about a third in 1953/54 to more than half in 1970/71, though it needs to be borne in mind that non-commercial fuels (firewood, charcoal, cow dung and vegetable wastes)





still account for nearly half of energy consumption and that relatively little is known or done about this major sector. Among commercial fuels petroleum consumed directly by final energy users accounts for nearly half the energy consumed while coal and electricity account for a quarter each. The mining and manufacturing and transport and communications sectors are the major users of commercial energy - 39% and 32% respectively. The share of agriculture though small - 10% - has grown rapidly in recent years with the spread of minor irrigation and the electrification of villages. All non-commercial and most of commercial energy consumed in India is derived from domestic sources. The major exception is petroleum where imports account for about 70% of consumption.

xxxii. The performance and expansion of India's fuel and power industries has acquired major importance as a consequence of the dramatic increases of world petroleum prices and the increasingly felt constraints on production of domestic energy sources. Presently coal is very much in short supply due to difficulties arising from congestion and limited line capacity in the coal-fields, the long distances involved in haulage of coal, the limitations of loading and unloading facilities, poor wagon utilization, and problems of operation including poor labor discipline on the railways. The Draft Fifth Plan proposes a major investment program designed to raise coal production from its current level of 80 million to 135 million tons by 1978/79. In the first year of the Plan the financial and foreign exchange requirements of this program are being fully met despite current resource constraints. Nevertheless, obstacles in the way of achieving the coal production targets will be difficult to surmount.

xxxiii. Whereas the annual demand for electric power has been growing at about 11% the supply of power during the Fourth Plan has been increasing at only about 6% per annum - a situation made worse in recent years by monsoon failures and consequent falls in hydroelectric power generation. A major expansion of generating capacity is proposed during the Fifth Plan from about 18,900 MW to 33,000 MW. This will be difficult to achieve. However, the improvements in project planning and execution, the reduced emphasis on hydroelectric projects with their long gestation period, and the increased efficiency of the domestic equipment manufacturers should permit achievement of 29,000 MW to 30,000 MW, by 1978/79 which would help alleviate the power shortage. The growth of the power system, the increase in the size of generating units, and the development of high voltage transmission methods, make it both practicable and desirable to plan future investments in terms of areas and systems larger than individual States. The establishment of Regional Electricity Boards which are advisory bodies was a small step in this direction, but it is officially recognized that much more needs to be done to ensure: (i) full development of interconnections between different entities; (ii) formulation of an accepted set of operating procedures, including agreed tariffs for transferring power between States, and (iii) timely exploitation of power resources which are shared among States.

xxxiiii. Particularly in the short-term the possibilities for reducing India's dependence on petroleum imports are quite limited not only because expendable uses are rare but also because alternate energy sources are in short supply. The substantial price increases introduced for gasoline and kerosene will probably go as far as is advisable towards curbing inessential uses of petroleum



products. Nevertheless, for balance of payments reasons a cut in consumption of petroleum products back to 1973 levels or even lower will be necessary. In view of the chronic shortages that now exist with respect to most forms of energy there is a strong case for making virtually all forms of fuel more expensive than at present. In the long run there are possibilities for increased efficiency in use of petroleum products as well as for substitution of alternate energy sources for petroleum provided the obstacles to coal production are overcome. Also in the long run the possibilities for stepping up domestic production of oil through new discoveries appear promising though this will call for substantial expansion of onshore and offshore exploration programs. Current efforts to enter into production sharing managements with foreign partners for exploration and development of offshore deposits could prove important in this context.

Transport

xxxiv. The Indian transport system has been undergoing fundamental change in recent years with increasing railway specialization in bulk long-haul freight and the transfer of much of the remainder, the high rated commodities, to road transport. This in combination with the slow growth in the economy has meant virtual stagnation in railway freight tonnage in recent years (although with longer average hauls) while transport on the roads has grown rapidly. Passenger traffic has had a sharp increase on both railway and road transport - much faster than passenger accommodation with a steady rise in congestion as a consequence.

xxxv. The railway emphasis of public investment in transport has continued in recent years in spite of the shift in traffic patterns from rail to road. Consequently rail investment in relation to traffic has increased, with reduced utilization of equipment in spite of large retirement of wagons. Conversely road development has lagged well behind traffic and the backlog of requirements especially for rural roads remains large. The uncertainties of future transport growth patterns make the assessment of the size and nature of transport investment requirements difficult especially now with the clouded economic outlook for the Fifth Plan period.

xxxvi. Transport investment priorities have been further complicated by the recent abrupt changes in the relative costs of fuels. This will undoubtedly require a reexamination of rail-road priorities and has already given added emphasis to the need for expansion of coastal shipping - especially for the transport of coal by ship from Northeastern India to the South and the West. The jump in oil prices relative to coal and the consequent increase in coal requirements has come at just the time when the railways are having increasing difficulty in moving coal, partly for organization and management reasons, but especially because of serious deterioration over the past year in railway staff and labor relations. This is a problem of critical relevance to India's ability to adjust with minimum difficulty to the adverse consequences of the oil price rise.

xxxvii. One bright spot in transport staff and labor relations in the past year was the settlement of staff-management disagreements on Indian Airlines



after several months of disrupted service. The settlement was on terms which promise improvements in the efficiency and economy of operations of the airline which were badly needed. A similar approach with similar results seems less promising in the greater complexities of staff and labor problems on the railways.

Domestic Resources

xxxviii. Among the difficult problems of the Fourth Plan, and its predecessors, has been the mobilization of domestic resources for development. India's revenue efforts have been consistently impressive but the problem of recent years has been rapid expansion of current expenditures - for the Bengal refugees, the Pakistan conflict, major drought relief, crash efforts to increase harvests, and rising pay levels. All this has affected the Fourth Plan strategy of reliance mainly on public saving to raise sufficient Plan financing on a non-expansionary basis. Actually the net national saving rate increased over the Plan period to about 12% of net national product - a return to the peak levels of the mid-sixties after a drop in the intervening years. However, the public saving rate remained about constant and because of this, total saving and the reduced supplement from net foreign assistance were less than Plan requirements in real terms. Furthermore they involved a substantial element of forced saving through Government deficits considerably larger than planned. The latter contributed to large monetary expansion and, in the context of severe material shortage, to rapid price increases in the past two years. The rate of increase in the wholesale price index in the past year was about 26%.

xxxix. In this situation Plan budgeting in the past two years has been austere with provision for Plan expenditures at constant or sagging real levels. The Plan allocation this year (adjusted to 1972/73 prices) is only about 10% of the Fifth Plan public sector program which is considerably below a level consistent with Plan objectives. Cuts have fallen most heavily on social programs. As a result of these and other cuts and further revenue measures the budgeted deficit this year has been greatly reduced from the Rs. 8 billion (10% of total expenditure) last year to only Rs. 1.25 billion this year. It will be difficult however to keep to this low deficit and something of further inflationary proportions, although not on the scale of last year's deficit, may materialize.

xL. On the monetary side, credit curbs have been imposed by the authorities in an effort to stem the monetary expansion which amounted in the past year to almost 15%. As yet however these measures have been of limited effectiveness.

* xLi. Broadly the key to India's domestic resource difficulties is an increase in material output which would contribute to both revenue and saving on the one hand and increase the availability of goods on the other. This, of course, depends a great deal on the weather and on the harvests as well as on other essential supply conditions which are not likely to be very favorable in the coming year or two. There is however the short term possibility of fostering both industrial and agricultural output through inducements to better use of existing capacity and effective distribution of available supplies and services according to output priorities.

The Balance of Payments

xLii. India's balance of payments difficulties and foreign exchange pressures are long standing but they have never been more acute than at present in the aftermath of the large increase in world oil prices and other essential Indian imports, and with large requirements of imported food. These developments have, unfortunately, sharply reversed the downward trend in the trade deficit from about US\$ 750 million in 1968/69 to a negligible size in 1972/73. This drop in the deficit was the result, however, of a deliberate and difficult adjustment to sharply falling net transfers of foreign aid from more than US\$ 700 million in 1968/69 to only about US\$ 200 million in 1972/73, and by a determination because of adverse and uncertain aid trends to protect foreign exchange reserves which rose from about US\$ 770 million to US\$ 1,310 million in this period.

xLiii. Last year as trade terms moved for the worse, so did the trade balance with a deficit of over US\$ 700 million in spite of a sharp rise in exports. There was fortunately a large increase in net aid transfers from both Consortium and non-Consortium countries which left reserves intact.

xLiv. This year import requirements are far larger because of the sharp rise in import prices, and uncertain financing prospects. On an austere basis, with the volume of most imports reduced to 1973 levels or below, the import bill would still be almost US\$ 5,000 million - nearly US\$ 1,500 million more than last year. Some help for financing this bill can be expected from larger export earnings because of buoyant world prices for many of India's exports. But with these import assumptions the total deficit would be about US\$ 2,400 (including debt service). This would require, if it were to be financed, additional Consortium and traditional non-Consortium aid as well as financings from other sources. In Chapter 10 a level of US\$ 300 million is assumed to be reasonable traditional non-Consortium assistance and the Consortium disbursements out of recommended new commitments of US\$ 1,400 million are estimated at US\$ 1,350 million on certain assumptions about the nature and quality of aid including a large measure of debt relief. This would leave a remainder of US\$ 750 million to be financed from reserves and transactions with the IMF and from other credits mainly from the oil producing countries. Prospects for the latter are now something over US\$ 200 million. On these bases the payment requirements for the current year may be manageable although with considerable difficulty, especially because of the austere import volume level that is implied.

xLv. Looking ahead, the problems of 1975/76 are not likely to be less difficult than those of this year, with continuing need for import austerity, for export effort, and again for large international assistance. Hopefully, next year's food import need may be a little easier, and terms of trade not quite so bad. But there is no reason at the moment for optimism on either of these counts.





xLvi. Beyond these early and unusually difficult prospects, much will depend in the longer term on balance of payments management and on future internal and external economic circumstances as they relate to the balance of payments.

xLvii. The keystone of India's past balance of payments management and a major element of development strategy has been import substitution. This has served to conserve foreign exchange, and has also developed strong support as a protection device. Cost considerations have usually been secondary and this has itself contributed to foreign exchange problems by weakening India's competitive capability in export markets. As an antidote, India has long had programs of special export incentives and this was one of the reasons behind the devaluation of 1966. Export incentives have continued and the depreciation of the rupee vis-a-vis various other currencies in the last two years has also encouraged exports. There is undoubtedly room for additional and better administered export incentives. Some also argue that the effectiveness of balance of payments management would be enhanced by further import liberalization to open India to world costs and technologies and expose Indian industry to the pressures for efficiency of world competition. This would undoubtedly be of benefit in the longer run to India's international competitive position. But in the interim a meaningful application of such policy would imply some increase in imports relative to exports until exports responded on the basis of an improved competitive position. The problem is that India has no margin for a relative increase in imports during this period while awaiting an export response. Nor is there margin for substitution of competitive imports within the present import pattern which consists exclusively of necessary raw materials and essential equipment and components.

xLviii. Probably the answer to this dilemma of transition from a highly import substitution orientation to a more export oriented outlook is that suggested in the Draft Fifth Plan - a policy based on complementarity between import substitution and export promotion. This would presuppose consideration for international standards and export promotion costs in setting acceptable limits to the domestic resource cost of saving foreign exchange through import substitution. It would also presuppose an effective program of export promotion to enhance the attractions of export markets vis-a-vis the domestic market.

xLix. In the past two years exports have done unusually well in current dollar values with an increase for the period of 30%. Both traditional and non-traditional commodities have contributed to the increase, especially cotton textiles, leather, oilcake, tobacco and coffee among the traditional items, and engineering goods, gems, clothing, marine products and handicrafts among the non-traditional. Most of this increase was due to higher prices, however, and only a small part to larger export volume. Essentially it was a reflection of booming world prices in which the benefits on the Indian export side have been far outweighed by increased costs on the imports side.

L. The limited volume element in export expansion lends emphasis to the need for greater export promotion efforts for both traditional and non-traditional commodities. Past policy has done a great deal to improve export incentives. But much remains to be done. A concerted promotional effort aimed

at alleviating the short-term physical and other constraints, at restraining domestic consumption, at permitting and providing for export to be a fully remunerative activity, and at facilitating the free movement of resources into those goods for which India has a comparative advantage has yet to be formulated.

Li. With India's export potentialities and a concerted export promotion effort it should be possible to reach the Fifth Plan objective of raising exports by almost 8% a year or even more. Nevertheless, with India's import requirements, the probable continuation of high import costs relative to export prices, the large external debt service, and on the internal side with continuing investment needs in excess of domestic saving there will be need for substantial foreign assistance for years to come. This year's gross external financing requirements are estimated at about US \$2,400 million, and continued need and availability of this order seems a reasonable assessment over the next five years. In a country with such vast poverty, with operations so close to the margin in every sector of the economy, with such limited resources to provide for economic and social necessities, and with the ever-present possibilities of natural misfortune, aid of the requisite size and quality has an important contribution to make to Indian development.



2. A.I.D. Assessment

The Bank report clearly contains all the elements of a comprehensive study of India's development progress. We are concerned however over the report's conclusions on 2 key points. First, the balance of payments figures for FY 74 and FY 75 imply a trade gap and aid requirement somewhat larger than we think likely. (Inter-agency discussions as well as discussions with Bank staff have been held on this question). Second, we take issue with the manner in which the Bank discusses the need for greater efforts on behalf of the government of India to improve its own performance - see issue 3 below (Tab E).



B. Issues for the U.S.1. Effect of India's nuclear explosion on our plans for aid.

India's nuclear explosion of May 18 has already had negative repercussions among aid donors. Canada has placed its non-food aid to India under review and other donors have expressed varying degrees of displeasure. Official U.S. reaction so far has been low-key and based on our general position against nuclear proliferation. The GOI's public rationale for the explosion is of course based on peaceful purposes (e.g. mining, stimulation of low-yielding oil fields, earth moving, irrigation, etc.). Moreover, the cost of the test appears to have been relatively small (\$10 million) in terms of its total FY 74 nuclear research budget (\$130 million) and its overall budget (\$11 billion).

Under the circumstances, a case can and should be made that such a use of resources by the GOI as part of its long-standing nuclear development program should not suddenly preclude our offer to discuss economic assistance. We have a long-standing interest in the stability and economic development of South Asian countries, and a humanitarian interest in preventing economic collapse or starvation - which overrides our concern about India's nuclear test. Moreover, any new U.S. aid to India will have to reflect areas of common U.S.-Indian interest, and focus on overcoming basic human problems.

To the extent this subject is addressed directly to the U.S. del, we recommend he state our belief that our position against nuclear proliferation and our humanitarian interest in helping to alleviate basic human problems are not contradictory.



2. Debt Relief

The World Bank is recommending to the Consortium debt relief equal to 45% of the service due from India in IFY 1974/75 to each national member of the Consortium. As of the date of this drafting (May 30) we have not received the Bank paper on this subject).

This recommendation is a modification of the proposal made by the Bank in a paper of February 19, 1974 which was discussed in detail at an earlier Inter-Agency meeting and which was the subject of a Consortium Working Group meeting in Paris, April 9, 1974. The earlier Bank proposal was for provision of Free Foreign Exchange equal to 50% of service due in the form of debt relief, untied aid, or local cost financing, or any combination of these, at the option of the donor. Many opposed this approach at the April meeting on the grounds that these methods were not precisely comparable and consequently inequities among donors might result.

The general reading of the April meeting was favorable to the provision of debt relief as well as increased aid (US and several others being silent or non-committal). Thus, except for the possible impact of India's nuclear explosion (at least one country will defer agreement to participate on this account) we would predict that the Bank's current recommendation of debt relief would be accepted by all or most other members.

Another potential issue which might divide the members is that of the basis of sharing. The Bank recommends each nation share in relief proportional to the service due it from India. Canada, UK, and the US have supported sharing formulas which discriminated in favor of the more-concessional lenders, but the Bank argues that that approach has served its purpose which was primarily to force attention to, and action to, improve current terms. On the other hand, France, Germany, Japan and Italy will object to anything other than proportional sharing. In the circumstances, we propose to reiterate US support for sharing which favors softer lenders, but recommend that we not, in the final analysis, make this an absolute sticking point. See attachment for discussion of Options.

1. Agree to participate, subject to agreement by others and to satisfactory understandings regarding non-Consortium donors (see below).
2. Decline to participate.
3. Indicate that our participation would be decided later.



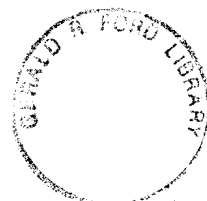
4. Agree to participate on a partial basis, perhaps at the \$29 million level of our share the past two years or some alternate partial figure.

Non-Consortium Creditors

India has, in the past six years of debt relief, repeatedly made the point that parallel debt relief from the Bloc countries should not be insisted on because its aid relations with the Bloc were merged in swing trade accounts and thus were not comparable with its aid/debt relations with the Consortium. Although unsatisfied with this reasoning, the Consortium has not pressed the issue.

The Bank, this year, suggests that, given the difference in form, a valid way of measuring Bloc and Consortium contributions was by examining the net transfer of goods. In recent years, the Bloc has received more from India than it delivered to India -- a net negative transfer. This was reversed to a net positive position in IFY 1973/74 by reason of the delivery of the first million tons of the Russian wheat loan. A positive net transfer from the Bloc is also expected for 1974/75 with the delivery of the second million tons of wheat, project pipeline drawdowns, and assumed new commitments.

While not totally satisfactory, the net transfer concept has some validity, and positive Bloc transfers to India give economic support as contrasted with the intolerable position of recent years in which Consortium debt relief could be said to have enabled India to be a net exporter to the Bloc. A minimum condition for US participation in a continuation of debt relief might be to seek explicit Indian agreement that positive net transfer from the Bloc was a necessary accompaniment to Consortium debt relief.



OPTIONS

1: fully support World Bank's rescheduling proposal

pro - a big economic boost for one of hardest hit LDCs

- positive indication of US interest in helping hardest hit LDCs
- possible favorable impact on bilateral Indo-US relations

con - strong Treasury opposition

- in view conflicting data, position difficult to defend solely on economic grounds
- potential Congressional opposition
- precedent for other hardest hit LDCs
- acceptance of proportional sharing without index of hardness
- remove major incentive for India to seek comparable non-Consortium relief

#2: reject Bank proposal and indicate we do not believe any debt rescheduling justified

pro -

con - same as in option 3, but with much greater likelihood it would be viewed in India as sharply adverse political signal

- conflict with other creditors would be heightened

#3: defer a decision on rescheduling citing the need to reconcile conflicting data

pro - improved balance of payments data would permit more accurate assessment of India's requirements

con - in era of volatile market fluctuations, "precise" economic projections are elusive

- unresponsive to fact that 1974 will be very difficult year for India
- inconsistent with positive U.S. approach in prior Consortium relief
- could be viewed as inconsistent with public US stance sympathetic to hardest hit LDCs



#3 (Contd)

- possible unfavorable impact on bilateral Indo-US relations

#4: support debt rescheduling at a lower amount than Bank recommends, with option to further review India's needs at a later date

pro - increased US flexibility in context bilateral Indo-US relations

- possibly attractive to countries, like Canada and Japan, where early support for more generous rescheduling has been tempered by India's nuclear test

- intensify pressure on India to seek greater East Bloc and OPEC assistance

- option to review India's needs at later date could be framed as positive approach

con - failure to achieve recommended rescheduling could intensify Indian reluctance to draw down reserves

- identification of US as principle obstacle to full acceptance Bank proposal could affect bilateral Indo-US relations

- possible conflict with creditors, such as UK, favoring full acceptance

Note: At the \$187 million level rescheduled last year, the U.S. share would be about \$43 million if shares were apportioned on the proportional basis being recommended by the Bank. If a determination of shares also considered an "index of hardness" the U.S. share would decline closer to the \$29 million assigned last year.



3. GOI Performance

At the April meeting, U.S. del said we agreed India's need for external assistance had increased, but "attention needs to be given by the Bank and India to internal policies and measures with both long and short-term consequences for development. We expect the Bank's annual report . . . will tell us more about how India plans to tackle its difficult problems."

The Bank's annual report does not fulfill our expectations. It mentions that greater efforts are required, for example, to curb population growth and improve utilization of existing fertilizer capacity, but it avoids recommending specific measures by stating, briefly, that the need is obvious. We would still like to hear more about the GOI's plans for improving capacity of fertilizer plants, developing such natural resource industries as coal and iron ore, promoting exports, and curbing population growth.

Under the circumstances, we recommend the U.S. del express our disappointment with the Bank report in this regard, and reiterate in a low key manner our interest in hearing how the GOI plans to tackle these problems.



4. Food

Food is one of India's most serious problems and may become critical even before the end of 1974. Domestic production of food-grains, instead of increasing to keep pace with population growth, has declined since 1971. The 1973/74 harvest shows an increase over the previous year but assuming it reaches 103 million tons, still falls short of the country's current need by an estimated 5 or 6 million tons. This means the GOI might need to import 5 million tons in 1974/75 although the World Bank indicates that the need is for 3 million tons. To the extent that their estimate is understated, India's need for aid is correspondingly understated. If the monsoon fails this summer, the import requirement will be much greater.

India terminated its drawing on U.S. PL 480 concessional sales after its record harvest of 1970/71. Ironically, in 1972, the monsoon failed badly and the government had to start purchasing grain again from the US (on commercial terms). In 1972/73 and 1973/74, purchases of grain (mostly wheat) from the U.S. reached about 2 million tons each year. Under present circumstances, we can expect the GOI to seek about the same amount of grain from the U.S. in 1974/75.

The GOI has asked us informally for concessional assistance (of an unspecified nature) for the purchase of U.S. grain in 1974/75. There is presently no PL 480, Title I grain set aside for India. On the assumption that additional grain will become available under Title I in the coming months, we have made the case that India should get 2 million tons - in effect concessional assistance for the 2 million tons the GOI will purchase in the U.S. anyway.

The above comments on the food situation are included here to underline the seriousness of this aspect of India's near-term needs, and to suggest that the U.S. del at the June meeting express our recognition of this fact.



India ConsortiumHistorical Background

The India Consortium is chaired by the World Bank and consists of the following 12 members: the U.S., U.K., Belgium, Canada, Germany, Italy, Netherlands, France, Japan, Sweden, Austria, and Denmark. Apart from infrequent "ad hoc" sessions to discuss special topics (e.g. population, debt relief), the Consortium members meet annually to review the Indian economy and give broad indications of their aid commitments within the framework of the Indian development plan. Some donors make specific pledges; the U.S. usually indicates amounts stated in its Congressional Presentation. The Consortium has always constituted by far the most important source of aid to India. Since 1958, more than 90% of both gross disbursements and net transfers have come from the Consortium. Since 1968 however, net transfers have declined steadily due in large part to the decline in PL 480 and other US assistance.

Aid from non-Consortium sources -- principally the USSR and Eastern Europe -- has been somewhat sporadic in its commitment and utilization and has usually been on rather hard terms (average grant element of around 40%). With only very small new commitments of aid from 1966/67 until late 1973, as well as slow disbursements, the net transfer from non-Consortium creditors was negative in each of the three years beginning 1970/71, the negative transfer reaching \$80 million in 1972/73. This situation has now been reversed by the Russian wheat loan of 1973; the net transfer in 1973/74 is estimated by the Bank to be about \$215 million.

Despite its declining role, the Consortium's gross aid has undeniably made an important direct contribution to India's economic development on two main counts. First, it has provided a crucial supplement to domestic resources and has thereby permitted higher levels of investment and consumption. Second, and in relative terms the more important factor, external assistance has financed a significant proportion of imports. Moreover, starting at the time of the Consortium's establishment, this support has been especially valuable at critical periods in India's development when the balance of payments has been under particularly heavy pressure. Without the Consortium's financial assistance, the Government's development effort would have been even more seriously held back than it actually has been through lack of resources.



2. U.S. Aid Statement

"In the context of a still-evolving economic relationship with India, we are seeking appropriations to enable us to provide development aid up to the level of \$75 million. In addition, we intend to continue providing food grant assistance valued at about \$45 million in FY 1975."

