INTRODUCTION

CLAUDIA WRIGHT*

The release of the US General Accounting Office (GAO) report on US assistance to Israel has stung the Israelis and their American supporters more sharply than they concede. The damage that has been done to Israel’s public posture in the US, especially in the politically unstable period into which Israel is now heading, is likely to be serious and permanent.

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This is not because of the specific classified information the unexpurgated draft report reveals. Most of these details have been known and widely published, if not in the US, then in the Arab world and in parts of the Israeli press. It is of interest to discover what details Israeli and US government officials have tried to keep secret from the American public on this occasion. It is also important in the American political context to have official US government substantiation that many Israeli claims—about the war in Lebanon, Israel’s role in Central America, the purposes to which Israel puts US financial assistance and military supplies—are bald-faced lies. However, this is not the first time we have had proof of the Israeli government’s mendacity.

The most important revelation in the GAO report is the disdain, even contempt which the Israeli government displays toward officials of US government agencies with whom they regularly deal, and on whom they materially depend. The GAO report shows there are many fundamental differences between Israeli and US officials—on Israel’s economic plans for financial stability; on the balance between Israeli and Arab military forces; on the threats Israel faces from its Arab adversaries and the requirements for defending against them; and on the likely impact on US business and markets of US-subsidized arms exports from Israel. The report also shows that Israeli officials intentionally mislead US officials in private, just as they lie in public, about these issues. They can usually do this without fear of private rebuke or public exposure because US officials allow the Israelis to censor the record of bilateral negotiations and suppress the evidence of policy differences.

The same American officials who disagree most strongly with the Israelis, as illustrated in the accompanying excerpts of the report, collaborated with the Israeli government to excise all sign of their disagreement, not only on the merits of the policy issues, but also on such elementary facts as the size of the US financial contribution to recoup Israel’s losses in Lebanon, and the extent of those losses.

In other words, it makes little difference to the Israeli government what US officials think of their demands for US assistance, or of the veracity of Israel’s economic and military presentations. The Israelis can count on their Congressional supporters to force officials to accede to their demands, just as they can rely on the US press to protect the Israeli position from damaging leaks by disgruntled US officials. These officials know that if they push their opposition to Israel’s demands too forcefully or openly, they run the risk of being targeted themselves—by campaigns of
Israeli-contrived leaks to the press, Congressional probing, and sanctions from their superiors in the Administration. The reaction to the release of the GAO report illustrates how this can happen.

When the censored version of the report was publicly released on June 24, 1983, the minister for economic affairs at the Israeli Embassy in Washington, Daniel Halperin, told the Washington Post (June 25, 1983) the report "strengthens some of the major points we have been making all along." The Near East Report (July 1, 1983), newsletter of the American Israel Public Affairs Committee, editorialized that "it confirms what Israel's friends have long been arguing: that US aid to Israel benefits this country in myriad ways, that Israel needs the aid if it is to repel the external threat to its existence, and that the program is well-run and efficient. . . . The GAO does not question the needs, the levels or terms of aid to Israel."

The release, a week later, of the uncensored document did more than embarrass the Israeli spokesmen by showing these claims to be false. It set off an alarm about American perceptions of Israeli manipulation in Israel itself. The government radio broadcast a statement on July 10 denying that "Israel succeeded in manipulating US presidents for many years in order to get its wishes . . . misled them, and did not always use the aid funds for their original purposes."

Then on July 11 it was revealed that parliamentary members of the Knesset Public Audit Committee had officially requested copies of the GAO analysis of Israel's foreign debts. The Committee members were reported as saying the GAO assessment might throw light on details which Israel's Finance Ministry had refused to provide the Knesset. A Committee hearing on the issue was scheduled, though this was to be held in camera for "fear that the leakage of information about Israel's foreign debts could harm future requests for credit," according to a Jerusalem television report on July 11.

The Knesset members were angry that details of Israel's foreign debt position, and of negotiations with the US to relieve it, might have been withheld by Israeli officials from the Knesset, in breach of Israel's parliamentary conventions and law. Members of the US Congress, however, were angry for just the opposite reason. They wanted to uncover and punish the US officials who had arranged the disclosure, enabling Congress to learn the details for itself.

On July 19, a group of eleven Congressmen, led by Larry Smith (D-FL) and Howard Berman (D-CA), formally asked the US Attorney General to order a Justice Department and FBI investigation "to determine whether
[release of the uncensored report] violates the law." Smith and Berman are first-term members of Congress and two of Israel's staunchest partisans on the House Subcommittee on Europe and the Middle East. They alleged that release of the report might constitute a case of espionage. On July 28 the Justice Department announced it was opening an investigation. The message for US officials was unmistakable—Israel could act through its Congressional supporters to punish US officials for doing no more than what the Knesset committees require of Israeli officials.

When the censored and uncensored versions of the report are compared, it is evident just how far the Reagan Administration and Congress have acquiesced in Israel's exaggerations of its military requirements, and in a gigantic scheme of chiseling US public funds to pay for them. Occasionally, US officials object to the chiseling. In September 1982, for example, the Israelis requested that the US Treasury authorize the transfer of a lump-sum payment of $713 million in Congressionally-approved assistance. The Israeli objective was to get the money in advance of military obligations or interest payments, invest it in an interest-bearing account, and draw the interest as additional income to add to Israel's foreign exchange reserves. Treasury Secretary Donald Regan refused to agree, noting that Congress had appropriated only the amount of the assistance, not the additional interest; that the assistance was voted for specific purchases of defense articles and services; and that the Israeli proposal would violate the law and Administration policy.

There was no official objection, however, to a complicated Israeli scheme to add to US assistance for the evacuation from the Sinai by acquiring US Corps of Engineers' equipment and materials, and reselling them in Israel, abroad, and back to the US itself. According to the GAO report, the Israeli government sought title, free of charge, to US construction equipment used in the building of the two new airbases the Carter Administration agreed to finance as replacements for the Sinai bases evacuated under the Egypt-Israel agreement of 1979. Although the US had financed the base construction and provided other redeployment assistance to Israel, the Israelis chiseled an additional $172 million in US-owned equipment which they took over, and then resold. The GAO estimated that about $1 million worth of this equipment could have been transferred directly by the US to its peacekeeping force in the Sinai. Instead, under the deal arranged by the Israelis, they acquired the equipment and the US Sinai force was obliged to buy it back.

Some of the figures provided for the first time in the GAO report sho
just how much greater the US deliveries of arms have been than previously published figures on Israel's inventory. The accompanying table illustrates the differences for several types of weapons. One reason for the discrepancy is that Israel resells many of the US weapons it receives on the international arms market. Unless formally authorized by the US government, such third-party transfers are illegal under US law and US-Israeli contracts. There is ample evidence, for example, of such illegal Israeli transfers to Iran since the outbreak of the Iraq-Iran war. In relation to the multi-billion dollar transfers of US aid to Israel each year, these examples are of relatively minor cost to the US budget, notwithstanding the reluctance US taxpayers would have to paying for them if they knew the truth. Their significance is that they illustrate the style of Israeli bargaining with the US, and the effectiveness with which Israeli officials get US officials to skirt the law, and Congress to look the other way. Secrecy is essential to maintain this process.

The contrasts between the censored and uncensored versions of the GAO report are striking, as the excerpts illustrate. But even more startling is the contrast in the reactions between Israeli and American parliamentarians confronted with the same case of leaked official secrets. In this affair, it is the US Congress which behaves as if its first loyalty is toward Israel, while it is the Knesset members who demand that their government tell the truth. It is precisely this which is the most damaging consequence of the GAO report.

Here is evidence of reasonable judgments by competent and experienced officials of the US Embassy in Tel Aviv, the State Department's Near East bureau, the Agency for International Development, the Central Intelligence Agency, the Defense Intelligence Agency, the Joint Chiefs of Staff, the Department of Commerce and other government agencies, as well as the independent GAO. They dispute factual claims by the Israeli government. They argue in favor of reducing US aid to Israel, of putting strict limits on the uses of US military assistance in Israel's defense industries, of denying Israeli requests for US investment and technology transfer for the Lavi fighter-bomber and other weapons systems.

Most significantly, there is evidence here of US officials arguing that US national interests differ from Israel's interests, that the US can be harmed by Israeli actions, and that reflexive backing by the Congress for Israel's demands is poor policy the Administration should not accept.

The evidence does not identify a group of anti-Israel, let alone anti-
Semitic officials within the US military and foreign policy bureaucracies. Many of these policy arguments have taken place before. However, it has never been so clear just how anti-American Israel’s supporters in the Congress have become.

### Israel’s Arms Inventory

<table>
<thead>
<tr>
<th>Weapon System</th>
<th>Official GAO Figure</th>
<th>Published Figure (1)</th>
<th>Percent Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tanks</td>
<td></td>
<td></td>
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<tr>
<td>— total all types</td>
<td>3,680</td>
<td>3,600</td>
<td>+2</td>
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<tr>
<td>— M-60s</td>
<td>1,406</td>
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<tr>
<td>Armored Personnel Carriers (APCs)</td>
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<td>Howitzers, self-propelled</td>
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<td></td>
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<tr>
<td>— M-109 155mm</td>
<td>393</td>
<td>320</td>
<td>+23</td>
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<tr>
<td>— M-107 175mm</td>
<td>144</td>
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<tr>
<td>First-line combat aircraft (excluding ‘trainers’)</td>
<td>665</td>
<td>574</td>
<td>+16</td>
</tr>
<tr>
<td>Improved-HAWK missiles</td>
<td>895</td>
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<tr>
<td>CHAPARRAL missiles</td>
<td>912</td>
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</tr>
<tr>
<td>Missile boats</td>
<td>24</td>
<td>22</td>
<td>+41</td>
</tr>
</tbody>
</table>

(1) Published figure obtained from various sources: International Institute for Strategic Studies, *The Military Balance* (annual); SIPRI Yearbook; and Anthony H. Cordesman, *Jordanian Arms and the Middle East Balance* (Washington, DC: The Middle East Institute, 1983).
[Editor’s Note: The following excerpts of the GAO Report are taken from the final, unclassified version, and from an uncensored draft version which was published by the American Arab Anti-Discrimination Committee (1731 Conn. Ave., NW, Washington, DC 20009). Sections which appear in medium type are the language of the final, unclassified report. Bold face type denotes the language of the uncensored, draft report.]

Foreign Military Sales (FMS) Assistance

Foreign military sales to Israel, the largest US military aid program, serves two major purposes. One is to indicate US political support for Israel and the other is to ensure the security of Israel by providing military equipment for its defense needs.

Israeli military needs and US political influences are both factors which determine FMS levels. The administration does evaluate Israeli military requirements, and the Congress also plays an important role. The Congress places more attention and exerts more influence on assistance to Israel than on other assistance programs.

Although its military has never been more modern and capable, Israel believes it has continuing modernization needs because of a potential Arab threat. Israel uses its FMS assistance for modern weapon acquisitions and other defense imports from the United States. Increasing US and Soviet arms sales to other Middle East countries has [sic] led to a spiraling effect on weapons sales and assistance levels.

The United States generally supports Israeli plans for its forces modernization, and agrees that there is an Arab threat to Israel. While Israel perceives the threat to be grave, DOD* officials believe that it is overemphasized at this time.

DOD believes that Israeli force modernization can be met at levels of $1.4 billion annually whereas Israel believes it needs higher levels of military assistance.

Development of Military Assistance to Israel

The United States has had a formal military assistance relationship with Israel since 1952, but did not become its major supplier of arms until after the Six Day War of 1967. The annual large US military assistance program began after the October War of 1973. In 1962, some US military loans were made and in 1966, the United States agreed to ensure the sale of arms to Israel, if not from Western sources, then from the United States. Hawk air defense missiles and A-4 fighters were sold to Israel but the major suppliers of military equipment remained: the British for tanks and the French for aircraft. After the Six Day War of 1967, France discontinued its aircraft sales and the United States began sales of the F-4 aircraft. US military assistance to Israel totaled more than $1.4 billion for fiscal years 1950 through 1973. In fiscal year 1983, the military assistance is $1.7 billion in grants and loans.

FMS Assistance Levels for Israel

Since 1974, Israel has been the recipient of more FMS assistance than any other country. Through fiscal years 1974 to

* DOD stands for Department of Defense. Also throughout, references to "State officials" means Department of State officials.—Ed.
1982, Israel received almost $13.5 billion in FMS assistance. Of this total, $5.4 billion was in the form of grants while about $8 billion was in long term loans. In fiscal year 1982, Israel was authorized $1.4 billion in FMS financing which was 33 percent of the total US military assistance program. Egypt obtained $900 million while all other recipients combined received less than $1.6 billion.

The administration proposed increasing Israeli FMS to $1.7 billion for fiscal year 1983 and Egyptian FMS to $1.3 billion. The Israeli program was proposed to include a grant element of $500 million and long term loans for the other $1.2 billion. The Congress approved $1.7 billion FMS assistance to Israel and raised the grant element to $750 million. Israeli documents show that US assistance funded 37 percent of its defense budget for fiscal year 1982.

According to the Central Intelligence Agency (CIA), Israeli expectations are that the United States will fund half of its defense budget.

Israel requested an additional $200 million in FMS assistance for fiscal year 1981 for financing additional redeployment costs associated with implementation of the Egypt-Israel Peace Treaty. The administration agreed, and made the request to the Congress, which added another $200 million and the FMS assistance level rose to $1.4 billion for fiscal year 1981. This same amount of assistance was continued into fiscal year 1982. In fiscal year 1983, due to the sale of the Airborne Warning and Control System (AWACS) and F-15 aircraft enhancements to Saudi Arabia, the administration requested a new level of $1.7 billion in FMS assistance and plans this level through fiscal year 1984. Officials in DOD and State Department believe that due to Congressional interest—$1.7 billion may become the new minimum for FMS to Israel.

Congressional Role

The Congress consistently views administration aid proposals for Israel favorably, and in recent years, has appropriated more aid for Israel than the President requested. When the executive branch requested a shift from the commodity import financing to cash assistance in 1978 the Congress earmarked Israeli security assistance to provide Economic Support Fund (ESF) on a cash basis, included larger amounts of forgiven FMS loans, and granted favorable repayment terms for arms purchases. For example, for fiscal year 1982, the Congress approved $50 million more in FMS grants than the administration requested. Again for fiscal year 1983, the Congress approved $750 million in FMS grants although the administration had proposed only $500 million in grants.

State and DOD officials say that it is not politically possible to submit to the Congress, as an administration proposal, a lower FMS figure for Israel than that for the previous fiscal year. The perception held by some DOD and State officials is that congressional approval for FMS is easier to obtain if increases to Israeli assistance are sought.

Foreign Policy Considerations

Many consider FMS assistance as a policy statement of US support for Israel. State Department officials noted that reduction in the program could trigger a crisis in political relations between
Israel and the United States. Arab States, as well as other countries and world institutions, might perceive that US support for Israel is waning if FMS levels were to be reduced. If the United States stopped providing FMS to Israel the consequences could be a halt to the peace process, a deterioration of Israeli military forces and economic difficulties leading to a request for military debt rescheduling.

We were told that decisions regarding FMS are made at the highest levels of the administration. Justifying FMS for Israel is seen only as an exercise by some lower ranking executive branch officials. The assistance levels are determined by policy considerations beyond those involving only basic defense needs.

FMS to Israel Linked with Egypt

The Egyptian and Israeli FMS assistance programs are politically tied to each other and are becoming more difficult to separate. The Egyptians have been requesting treatment similar to the Israelis since Camp David. This is reflected in higher levels of assistance, similar terms of FMS repayment, similar uses of cash flow, and similar desires for advanced equipment. The Israelis, on the other hand, desire that the United States maintain its special relationship which means favorable treatment. In Israeli eyes, the linkage is eroding part of their special relationship.

Israeli Military Needs

US and Israeli officials agree that Israel has security problems which require FMS assistance. However, there is growing concern in Israel over the level of FMS due to: increasing US arms sales to Arab countries; erosion of its qualitative advantage; and Israeli force modernization needs. Nonetheless, DOD officials generally believe current FMS levels are sufficient for Israel's needs.

...Israeli Concerns for Threat from Region...

Israelis are particularly sensitive to the level of casualties they might sustain in a full-scale war with the Arabs. The efforts to modernize Arab States such as Saudi Arabia and Jordan to improve their military capability to meet threats from Iran and Syria and to deter Soviet expansion also expand the Arabs' potential capability against Israel. CIA believes this could exacerbate Israeli concerns about the Arab threat and could foster Israeli preemptive attacks in future crises.

Although some of Israel's potential adversaries are obtaining the same generation of technologically advanced weapons, US officials point out that Israel retains greater operational effectiveness of its forces. This is attributable to superior leadership, morale, training, motivation, and the ability to employ and maintain advanced technology weapons, acquisition and integration of command, control, and intelligence systems complement Israel's ability to employ its forces more effectively than the Arab states. CIA, however, notes that the numbers and quality of weapons and support systems likely to enter Arab inventories and their improved availability to use them may gradually begin to narrow Israel's qualitative edge near the end of the 1980s.

Some State Department officials believe that the qualitative gap is already getting smaller between Israel and the Arabs and agree that US assistance is helping to narrow the gap. DOD analysts point out that the
methodology in determining qualitative edge is not precise and that it is difficult to determine what exactly tips the balance. DOD officials stress, however, Israel's ability to use the equipment more effectively and that it has always defeated the Arabs. Thus, DOD officials noted that, although US arms sales do represent problems for Israel, it can maintain its qualitative advantage. Moreover, the President has assured Israel that he is determined to see that it maintains its qualitative technological edge.

Differences in View of the Threat

In general, US officials agree with Israel that the Middle East is a very unstable area and will continue to be so for the foreseeable future. Both countries agree that there are Arab States which pose a potential threat to Israel. However, the United States does not concur with all Israeli assessments concerning the threat.

Israel views its immediate threat as the military forces of the combined armies of Syria and Jordan, aligned with additional forces from Saudi Arabia, Iraq, and the other Arab countries. Syria and Jordan are seen as direct confrontational states, as well as Saudi Arabia. Iraq poses less immediate concern for Israel but it expects a substantial Iraqi presence in any potential conflict. According to Israeli military planners, Egypt remains a potential threat. Israel says it has to have an Egyptian scenario because the treaty has not been sufficiently tested by time and events and the unstable character of Arab governments in the Middle East.

The balance of military forces between the Arabs and Israel is considered to remain in the Arabs [sic] favor by Israeli military planners. Additional Israeli concern is voiced over Western and Soviet weapon systems sold to the Arabs.

The United States believes Israel faces less of an Arab threat. The US position is that there are moderate Arab states which include Egypt, Jordan, and Saudi Arabia. However, Israel does not agree that these are moderate Arab States. CIA estimated that another combined Arab-Israeli war is unlikely in the near future because of (1) the general disarray in the Arab world and the effects of the Iran-Iraq War, and (2) weapons ratios are now better for Israel than they were in the October War in 1973.

Although Israeli military planners informed us that they could defend Israel with weapons ratios that were 3 to 1 against them, they noted that the combined Arab weapons inventories exceed this ratio. US officials point out that Israeli military projections are unrealistic in that they include every weapon in all the Arab countries as part of the ratio of arms lined up against Israel.

The Quantity and Quality of US Economic Support

Israel had been receiving a mix of ESF grants and loans until fiscal year 1981, when the Congress started authorizing all grants for the Israeli ESF program. The Congress has favored all grants since that time despite administration proposals to convert back to a mix of two-thirds grants and one-third loans. For fiscal year 1983, the Congress approved $785 million in ESF grants to Israel. The administration request to the Congress in fiscal year 1984 will be for all grant ESF.
Determination of ESF Levels

Since ESF aid to Israel is not tied to specific development projects, its purpose has been expressed by the administration in various ways such as to (1) maintain economic stability and a modest level of growth, (2) provide balance of payments support, and (3) import certain civilian goods and services without high cost commercial borrowing and foreign exchange reserve drawdowns.

Israel, in its latest aid request to the United States, requests that economic aid be granted at a volume sufficient to cover a major share of its financing gap of $1.2 billion. The request points out that whatever Israel cannot generate from its own resources or from US assistance, it must obtain through short-term borrowing. A recent CIA study points out, however, that Israel could use its foreign exchange reserves or, if needed, could take further domestic austerity measures to decrease imports.

Because ESF is not project tied, the amount of aid is based on political considerations and some economic analysis. The US Embassy, in commenting on Israel's 1983 aid request, gave its view that continuance of aid at the same levels as in fiscal year 1982 appeared to be the best course of action from both a political and economic point of view. While showing an undiminished US support to Israel's creditors, the US Embassy reported that the aid in real terms would be lower which might provide extra incentive for Israel's economic policymakers to restrict public as well as private consumption. In its assessment of Israel's fiscal year 1984 aid request, the Embassy essentially repeated these same views.

The Embassy felt that any reduction of ESF would be impractical both economically and politically. Economically, it was expressed that Israel's economic stabilization programs would be damaged and it would hurt the country's chances to obtain foreign exchange from commercial sources. Politically, it was believed that such an unprecedented occurrence would be interpreted as a reduction in overall US support, could adversely impact on future peace efforts, and could affect broader US goals in the entire region.

Continuing, the Embassy said that an increase in aid would assist Israel economically and demonstrate that, even with disagreements between countries, the United States has not changed its commitment to Israel. However, it believed that arguments against higher aid levels were more compelling. First, Israel could manage at current assistance levels. Secondly, increased aid would remove some of the urgency that exists for an economic austerity program. Also, increased levels might damage Israel's standing within US public opinion where reductions were taking place in domestic US programs and in other foreign aid programs.

US Assessment of Israeli Goals

US assessments cast doubt on Israel's ability to reach its economic goals as quickly as it anticipates. According to a May 1981 report, the goals of reducing real spending and curbing real wage gains by Israel's unions are particularly important and equally difficult.

The US Embassy, in a more recent assessment of Israel's economic projects through 1986, also cast doubt on the
availability [sic] of the country to realize the benefits associated with its "overly optimistic" analysis as quickly as anticipated. The worldwide recession prevented Israel from reaching its export goals in fiscal year 1982 and, although the country is capable of quickly shifting production to export markets, Israeli exports may not recover as rapidly as forecasted if the recovery of Western economies is slow.

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Israeli Debt Servicing Requirements for Defense Purchases

In fiscal year 1982, Israel paid $722 million for defense loans to the United States. Although ESF is not intended to service FMS debt, in theory, the amounts have been such that Israel has been able to cover its US military debt repayments with cash transfers under the ESF program.

Israeli military debt repayment will rise from a projected $887 million in fiscal year 1983, to about $1.1 billion in fiscal year 1992. In an earlier report we found that for the next several years, Israel appears likely to be able to repay its FMS obligations (mostly interest) but could encounter debt servicing problems when it also begins to pay large principal payments after the expiration of its grace periods. Principal payments will continue to mount as the grace period for each succeeding year's program expires. In 1983, Israel's FMS debt is projected to be 84 percent of its total debt to the United States. The sheer size of Israel's FMS loan payments (projected to be over $900 million annually) combined with factors affecting its balance of payments prospects could alter Israel's ability to service its debts. Such factors were identified by AID in its 1982 report on Israel's economy and debt repayment prospects as

— the price of imported energy,
— economic conditions in the countries with which Israel trades,
— political and military developments in the Middle East and their impact on Israel's defense spending, and
— the rate and pattern of growth in the Israeli economy.

Of the $875 million which Israel owed the United States in 1982 for debt servicing, $810 million, or 93 percent, is for defense loans. Israel has been able to cover these US military debt repayments with the cash transfers it has been receiving under the ESF program. Now this situation is changing since grace periods are starting to come to an end for previous FMS loans. Thus the period of postponing Israel's defense costs is over and the impact of a large and unrealistic FMS loan program must be faced. Unless the amount of ESF is greatly increased, the difference will worsen as the decade of the 1980s continues.

To analyze the severity of Israel's debt servicing requirements, we projected the defense loan repayments coming due as compared to accounting ESF levels of $785 million per year. We found that the difference between this level of ESF and the security assistance repayments will continually increase each year from $189 million in fiscal year 1983 to approximately $955 million in fiscal year 1993. Israel will face the fastest rate of increase in its security assistance repayments during this period since the termination of grace periods will accumulate.

As noted earlier, even with a general
recovery of the world market for exports, it would appear doubtful that Israel can realize its optimistic forecast for export growth to help pay for this rising debt burden. If Israel were to use its foreign exchange reserves, its credit rating in the international commercial market could be adversely affected and, if it increased commercial borrowing, it would only shift the debt from the US Government to the commercial market which has shorter repayment periods and higher interest terms which would heighten the overall debt in later years. Thus, Israel is more likely to make further requests that the United States assist by increasing its economic support.

Even if the United States increased its economic assistance to maintain fiscal year 1982 purchasing power, a substantial deficit would still result. In addition, since there is a political linkage between aid to Israel and Egypt, the Congress would also have to consider the double budgetary impact of such a step. The Congress could decide to increase ESF to fully cover the debt servicing requirements as has been proposed. However, opponents of such a proposal say that the United States would run the risk of highly increased Israeli FMS requests. Additionally, Israel would thus avoid incurring the financial impact of repaying FMS loans that calls for prudence in its spending. Furthermore, this could also set a precedent for other countries to request the same treatment.

Other options for Israel include seeking more concessional loans, a greater amount of forgiveness in its FMS loan program, or further expansion of the grace period for FMS loans. Israel has already asked that the United States revert back to the one-half forgiven credits and one-half loan formula for FMS aid as was done prior to fiscal year 1981. These steps, of course, would result in additional costs to the United States.

A 1982 US study on the overall balance of payments problem and debt servicing situation drew similar conclusions. The study included a projection of all debt repayment; military imports in excess of US military assistance; and civilian imports over exports. Given current financial policies, it concluded that the gap in Israel's civilian imports over exports will worsen dramatically in the next few years and that, given Israel's present procurement plans, its military deficit will also grow as defense imports outstrip US military aid. Additionally, it was believed that this deficit could grow substantially if the Israelis move to replace equipment lost or damaged during the Lebanon campaign. Because unilateral transfers (excluding US aid) and Israeli bond sales do not normally respond to economic crises, the study concluded that a large projected financial gap will probably force the Israelis to press for additional US aid or to implement austerity. However, the study concluded that Israel would only resort to a major austerity program if there were no other options. Rather, Israeli policymakers prefer to make up the difference through increased US aid or, alternatively, commercial borrowing.

Nonetheless it would appear that the United States may face greater pressure regarding the amounts of aid to Israel and the conditions with which it is granted.
Economic Impact of the Lebanon Crisis

According to Israeli officials, the Lebanon campaign will not result in any increase in aid requested from the United States. However, there is a substantial foreign exchange component directly related to these activities which increases Israel's balance of payments deficit. This increase to Israel's foreign exchange needs can have an effect on its request for ESF since the request is based on an analysis of total foreign exchange needs regardless of source.

Israel divides the cost associated with the Lebanon campaign into two categories—direct and indirect—which are to be funded over a 3-year period. Direct costs include the loss, damage to, and amortization of equipment; the maintenance of reservists; and public works and transportation related to the operation. Direct costs are divided by Israel into those which can be financed domestically and those which require foreign exchange (i.e., imported goods). The indirect costs are measured in terms of the loss of production. According to preliminary information provided by Israel, the costs are estimated as follows:

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<th>Costs Type</th>
<th>Cost (in millions)</th>
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<td>Domestic component</td>
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<tr>
<td>Foreign exchange component</td>
<td>350</td>
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<tr>
<td>Indirect Costs</td>
<td>200</td>
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<td>Total</td>
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The $650 million direct costs are to be financed domestically over a 3-year period from budgetary cuts, an increase in the value-added tax (from 12 to 15 percent), the imposition of a 3-percent import levy, a compulsory loan from wage earners and companies, and a tax on stock market transactions. In its current aid request, the Government of Israel has indicated that it would like to use larger amounts of FMS for domestic defense-related purchases than it had previously projected. It is possible that this increase is to cover war-related expenditures. On the other hand, the increase may result from other considerations, such as inflation or a shift in the types of items which Israel plans to produce domestically. US reports indicate, however, that the increased aid and better terms requested by Israel in its current aid submission include compensation for its losses during the Lebanon campaign.

The remaining 35 percent, or $350 million, represents the foreign exchange component of the direct costs which are to be financed over the next 3 years, half from private sources abroad (bond sales and the United Jewish Appeal) and half from commercial borrowing. However, the increase of $50 million in Israel's request for FMS reflects, at least in part, aid for the replenishment of ammunition stocks drawn down and tanks lost during the fighting in Lebanon.

The estimated $200 million in indirect costs does not include substantial tourism losses. These losses began prior to the Lebanon campaign and for the most part can be attributable to the international economic situation. For example, in June 1982, there were 22 percent fewer tourists than the year before. Using this as a basis, Israel's estimated loss in foreign revenues would be about $100 million during its fiscal year 1982. Inclusion of this component would increase Israel's total foreign exchange needs associated with the campaign to approximately $475 million (the $350 million plus the $100 million and another $25 million which Israel had already included under indirect costs for loss of exports).