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SPECIAL MEMORANDUM

BOARD OF
NATIONAL ESTIMATES

The Shah's Increasing Assurance

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7 May 1968
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CENTRAL INTELLIGENCE AGENCY

OFFICE OF NATIONAL ESTIMATES

7 May 1968

SPECIAL MEMORANDUM NO. 9-68

SUBJECT: The Shah's Increasing Assurance*

SUMMARY

During the past decade the Shah has emerged as a self-confident potentate, determined to assert his and Iran's prerogatives against all comers. In the economic field he will continue to press the consortium of Western oil companies vigorously for vast amounts of revenue to fund Iran's economic advance, but eventually mutual interest in maintaining oil production will probably lead both parties to an acceptable compromise. Abroad, his determination to extend his influence in the Persian Gulf as the British depart is likely to maintain continuing tension in his relations with Saudi Arabia. As in the past, the Shah will seek arms support from the US, and his increasing feeling of independence will make for occasional friction between the two countries, though the Shah will continue to value his association with the US.

25X1



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1. During the past decade the Shah has dramatically strengthened the position of the monarchy in Iran. Top government figures who had, or who aspired to, an independent power base have been cut down. Parliament, too, has been transformed from a body representing the interests of landlords to one whose members are nonentities owing their position exclusively to his favor. At the same time, the Shah has undercut the already fragmented opposition by carrying out economic and social reforms it has favored. Moreover, his economic and military deals with the USSR have won him recognition at home as the foremost defender of Iran's national interest and as the personification of Iranian independence in the international sphere.

2. In scoring these achievements, the Shah has often acted against US advice. As a result, he attributes his considerable success largely to the correctness of his policies and to his own skill in political maneuver. This belief has transformed the Shah from a timorous, titular monarch into a selfconfident potentate, determined to assert his and Iran's prerogatives against all comers. This was symbolized by the elaborate coronation which the Shah staged in October 1967.

- 2 -

S-E-C-R-E-T

3. The Shah's design for Iran is based on economic rather than political development. The original emphasis placed on rural uplift by the so-called "White Revolution"* in 1962 has lately been supplanted by a focus on industry as well as infrastructure projects -- especially dams and transportation facilities. The distribution of land called for in the Shah's reform program has been essentially completed; he is now content to leave the more difficult task of increasing agricultural productivity to the technicians who have come increasingly to staff the important positions in the bureaucracy. The Shah sees rapid industrialization as essential not only to increase prosperity and national well-being, but also to provide an outlet for the energies of educated Iranians who might otherwise prove troublesome for the regime. Over the long term this will probably not provide a satisfactory substitute for greater political participation, but for some time to come the unrest of earlier days seems under control.

* The name given to the Shah's six-point program of land reform, profit sharing for workers, eradication of illiteracy, electoral reform, nationalization of forests, and the sale of government enterprises. It was subsequently broadened to include the Health Corps, the Development Corps, the village court system, nationalization of water resources, regional development, and a program to increase administrative efficiency in government.

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4. To carry out these economic projects the Shah has sought, and is receiving, some help from foreign quarters for these projects. But as many of these endeavors will not yield early returns, Iranian industry will require continuing large inputs of foreign capital for some time to come. Iran's rapidly rising oil revenue is the most promising source for this capital, and the Shah is determined that Iran get as much as possible. Indeed, the doubling of oil revenues in the past five years has been largely responsible for reinvigorating the non-petroleum sectors of Iran's economy. The Iranian government has pledged to devote about 80 percent of its oil income to economic development. The Shah is now demanding that the consortium of Western oil companies increase their liftings to guarantee Iran a total income of \$5.9 billion over the next five years -- a sum which would mean an average increase in revenue of 15-20 percent a year. The companies have resisted his demands, refusing to promise a total income of more than about \$4.5 billion over the five year period. After pressing the companies vigorously to meet his terms, the Shah recently accepted production levels for the year 1968 which would produce revenues of about \$40 million less than the \$865 million he originally sought.

- 4 -

S-E-C-R-E-T

5. Although the Shah has backed down somewhat in his immediate demands, the issue is far from settled. Negotiations are scheduled to resume in October 1968 regarding production for 1969. At this time the gap between the Shah's desires and the companies' offers will be far greater than in the past. The Shah's prestige is visibly engaged in this bargaining process -- the announcement of the 1968 settlement was couched in ambiguous terms to conceal the Shah's retreat -- and he will no doubt press the companies even more than in the past. The companies would prefer to expand production of cheaper oil in other countries and they too, are reluctant to give in. But both parties find oil production in Iran profitable and at bottom neither side wishes to precipitate a break. Thus, after long-drawn out negotiations and growing acrimony the parties are in the end likely to find an acceptable compromise.

6. The Shah's foreign policy is based on assertion of Iranian independence; he wants to appear less publicly lined up with the West, although he has no interest in abandoning his basic Western orientation. On the other hand, he is no longer greatly worried about the Soviet threat and he recognizes the political and economic benefits of improving relations with the USSR. He has, therefore,

concluded economic deals with the Soviets, principally an exchange of over \$1 billion of natural gas for a steel mill and other items. He has even purchased military equipment, including some weapons though not of advanced types, from the USSR under a \$110 million agreement and might buy more if he cannot get what he wants from the West on favorable terms. Nevertheless, it will be difficult for the USSR to translate this into political influence, and the Shah is likely to react strongly if the Soviets appear to be interfering in Iran's domestic affairs or otherwise threatening his interests.

7. As his fear of the USSR has receded, the Shah has come increasingly to focus his concern on regional affairs. Since the UK's announcement of its intention to leave the Persian Gulf by 1971, he has been particularly interested in that area. In keeping with his nationalist pretensions, the Shah is determined not to permit any outside power to play an influential role in the Gulf after the British leave. UAR withdrawal from Yemen and the resounding Egyptian defeat in the June war with Israel have made the Shah somewhat less fearful of Nasser's ability to foment troubles in the Gulf. Nonetheless, he still regards Arab nationalism as a threat to his position. He therefore feels impelled to expand

- 6 -

S-E-C-R-E-T

his influence over the emerging states on the Arabian Peninsula, and his aspirations may have been stimulated by his confidence that no country in the Persian Gulf can match Iran's power.

8. The Shah's ambitions in the Gulf are disturbing his relations with Saudi Arabia and the smaller states of the area. While the Shah probably has no serious designs on the western littoral of the Gulf, he is insistent on pressing maximum claims to undersea oil deposits. He had initialled an agreement with Saudi Arabia defining a median line in the Gulf, but it thereafter developed that the area on the Saudi side has large oil reserves. Hence he has recently repudiated the agreement, and some of his lieutenants -- though perhaps without his knowledge or consent -- went so far as to seize an Aramco rig which was attempting to drill in this disputed area. The Shah, however, has stated that he will not resort to such forceful tactics in the future.

9. Nonetheless, he has created new controversy by raising heretofore largely dormant claims to Bahrein; he is also pressing the British to cede the tiny islands of Tunb and Abu Musa at the mouth of the Persian Gulf -- held by the Trucial Shaikhdoms of Ras al-Khaima and Sharja. His demands for Bahrein are probably

advanced as a bargaining counter in his campaign to increase his share of the Persian Gulf seabed, but he may be more serious about the other islands. Yet even though the parties recognize the desirability of an early settlement of the issues between them, they are not likely even to begin serious negotiations for some time. Both King Faisal of Saudi Arabia and the Shah are reluctant to appear to be backing down by taking the first step toward talks. In this situation, the Shah and Faisal will remain at loggerheads and tension in the area is likely to continue.

10. The Shah's military policy has also complicated his relations with the US. Iran has for the past several years been pressing to purchase substantial quantities of modern weapons, originally on the grounds that they were needed to protect against Nasser; the Iranians now claim that these arms are required to insure stability in the Gulf area. Indeed, it was US refusal to extend credit for this equipment in 1966 that provoked the Shah to conclude a \$110 million arms purchase agreement with the USSR. The Shah is now demanding from the US a commitment for \$600 million in military credit sales to Iran over the next five years to buy naval craft as well as advanced aircraft and ground force equipment. He has threatened to turn to other foreign suppliers -- including

- 8 -

S-E-C-R-E-T

the USSR -- if the US is unwilling to accommodate his demands; Iran has ample resources of foreign exchange to make good this threat without any serious effect on its economic development pace.

11. The Shah would probably be willing to accept a US commitment for somewhat less than his total demands, as long as no major categories of equipment were excluded entirely from the agreement. On the other hand, he would have little compunction in seeking equipment from European sources to make up any shortfall in US supply. He might even increase his purchases from the USSR, though more likely of relatively unsophisticated arms than of advanced weapons systems. In any event, the problem of arms will be a recurring one. The Shah's increasing feeling of independence will make for occasional friction between the two countries, though he will continue to value his association with the US for a variety of reasons, including its use as an offset to Soviet influence.

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