POLITICAL SUMMARY

HISTORICAL BACKGROUND

Brazil was discovered in 1500 by the Portuguese explorer, Pedro Alvares Cabral, and was subsequently settled by the Portuguese, motivated principally by the lucrative Brazil-wood trade. The first successful settlements were at São Vicente near the present city of Santos and on the northern coast of Pernambuco. In 1630 a Dutch colony was established in Pernambuco but was driven out by combined Brazilian and Portuguese forces in 1654.

The first major exploration and settlement of the interior of Brazil began in the 16th century when bands of pioneers called "bandeirantes" moved westward from São Paulo, seeking gold, precious stones and Indian slaves. These bands explored virtually all of western and southern Brazil, took possession of the Amazon region for the Portuguese crown and founded what are today some of the major cities and towns in the states of Minas Gerais and São Paulo. Subsequently, the growing economic importance of cattle raising contributed further to the settlement of western Brazil, and this process of exploration and development still continues.

Although sporadic revolts occurred against Portuguese rule after the first such attempt in 1779, the migration to Brazil of the Portuguese royal family under Prince Regent Dom João VI in the early 19th century as a result of the Napoleonic invasion of Portugal and the fact that Brazil thus became the seat of the Portuguese Government, helped to strengthen the position of the mother country here. Nevertheless, in 1822 after the return of Dom João VI to Portugal his son, who had remained in Brazil, declared Brazil independent from the mother country and became Emperor Pedro I of Brazil. He was forced to abdicate in 1831 in favor of his son who, after a ten-year regency period, mounted the throne as Emperor Pedro II in 1841. During his long reign of forty-nine years, which was characterized by stability and good government, the groundwork was laid for the country's subsequent economic and political development. Slavery was abolished by executive decree in 1888.

Notwithstanding the benevolent and relatively efficient government which Brazil enjoyed under the monarchy, increasing republican sentiment led to the downfall of the Empire in 1889 and the promulgation in 1891 of a republican Constitution markedly similar to that of the United States.

The new republic was governed under this Constitution until 1930, when a successful revolution installed Getúlio Vargas as President and a new Constitution was drawn up. In 1932 the State of São Paulo revolted in a movement which developed secessionist tendencies, but the revolt was put down by the federal forces. In 1937 Vargas established by decree an authoritarian regime which was known as the "New State." Under this regime a new Constitution was promulgated and Vargas became a virtual dictator. The "New State" was overthrown by a military movement in 1945, and a new Constitution which is still in effect was established the following year.
Eurico Gaspar Dutra served as President from 1945 to 1950. In 1950 ex-President Vargas was again elected to that office in which he served until August 1954 when he committed suicide. He was replaced by Vice-President João Café Filho.

In the presidential elections of October 1955, Juscelino Kubitschek de Oliveira, ex-Governor of Minas Gerais, was elected President. His running mate, João Belchior Goulart, was elected Vice-President.

In November of the same year, President Café Filho suffered a heart attack and relinquished his duties temporarily to Carlos Luz, the Speaker of the Chamber of Deputies. Within three days Luz was removed from the presidency by the Army. With congressional approval, on the ground that he was conspiring with military elements to prevent the installation of the Kubitschek-Goulart Administration. After President Café Filho's recovery, the Congress on November 21 refused to permit him to resume the presidency and the President pro tem of the Senate, Nereu Ramos, became Acting President. The Kubitschek-Goulart Administration took office on January 31, 1956.

In October 1960, Janio Quadros, former Governor of the State of São Paulo, was elected President by the largest majority ever received in Brazil's history. Vice-President Goulart was re-elected. The Quadros administration took office in January 1961.

On August 25, 1961, Quadros resigned from office and Speaker of the House Ranieri Mazzilli took over as interim President, while leading civilian and military authorities sought a satisfactory way out of the unprecedented crisis. A Constitutional Amendment enacted on September 2 established a parliamentary form of government; and on the same day it was announced that Vice-President João Goulart would replace the outgoing Quadros for the remainder of the presidential period (through January, 1966). The amendment also provided for a subsequent general referendum on which system of government would prevail in the future. The referendum is scheduled to take place on January 6, 1963.
Structure of Government

Like the United States, Brazil is a Federation of States (twenty-two states, one Federal District and four territories). It is governed under a Constitution promulgated September 18, 1946 and amended on September 2, 1961. Its official name is the Republic of the United States of Brazil and has been so ever since the Constitution of 1891, which established the first republican government, replacing the deposed monarchy.

The 1946 Constitution provides for a rather detailed distribution of powers between the Federal Government and the States, including, unlike the United States, a mutually exclusive division of the taxing power. Federal powers are more numerous and broader than in the United States. Not only is the federal power supreme in the fields of major national interest (economic policy, labor relations, etc.), but also, for instance, most legislation on general and permanent subjects is federal (criminal law, domestic relations, business law, etc.). Despite this, however, in everyday domestic politics and even in the formulation of the Government's policies, the Brazilian States, or rather, the administrations in power in several of the more important of them at any given time, often carry more weight than do the state governments in the United States.

The so-called "additional act" or constitutional amendment which was promulgated on September 2, 1961 established a parliamentary form of government (the first in Brazil since the end of the Second Empire in 1889). Specifically, this amendment established a Council of Ministers responsible to the Congress, named Vice President João Goulart as President of the Republic until January 1966 and provided for a subsequent popular referendum to decide the question of retention of a parliamentary system of government or a return to a presidential system. Such a referendum is scheduled for January 6, 1963.

The legislative branch of government is bicameral, with a Federal Senate and a Chamber of Deputies. The Senate consists of three senators from each State and from the Federal District, elected from a term of eight years, two-thirds and one-third of the Senate being renewed every four years, respectively. The members of the Chamber of Deputies are elected for four years on the basis of each State's population with a minimum of seven members for each State, and with representation also from the Federal District and four Territories (excluding the Territory of Fernando de Noronha which is under military administration). With the shifting of the Federal District to Brasília in 1960, the new State of Guanabara was created out of the former Federal District.

There is no system of federal courts as in the United States. The only federal courts are the Federal Supreme Court, one Federal Court of Appeals (which generally is concerned only with matters in which the Federal Government has pecuniary interest), and courts for special problems, such as the Labor Courts and the Electoral Courts.
In general, federal laws are administered by the state courts.

**Political Events since 1955**

In the presidential elections of October 1955, Juscelino Kubitschek de Oliveira, ex-Governor of Minas Gerais and a member of the Social Democratic Party (PSD), was elected President on a coalition ticket. His running mate, João Belchior Goulart, National Chairman of the Brazilian Labor Party (PTB), was elected Vice President.

Due to the unsettled circumstances in which it came to power (see "Historical Background"), the Kubitschek Administration (1956) was subject to recurrent crises during its first year in office. In 1957 and 1958, however, the Administration achieved a greater degree of political stability. The congressional and state elections of October 1957 were notably orderly. During 1959-1960, despite some recurrent social strains reflecting increasing economic difficulties, plus tensions arising from the 1960 presidential campaign, the Administration continued to consolidate its position and President Kubitschek continued to gain in prestige. Factors in this trend were the appeal made to Brazilian national pride by the President's spectacular achievements in the creation of Brasilia (inaugurated as the new Federal District on April 21, 1960), the construction of highways traversing the Brazilian interior, and the fostering of new industries (of which the automobile industry is particularly noteworthy).

In the presidential elections of October 1960 the opposition candidate, Janio Quadros - supported by the National Democratic Union (UDN), the Christian Democrats (PDC) and two other small parties - won a landslide victory over the "government" candidate, former War Minister Marshal Henrique Teixeira Duffles Lott - supported principally by the Social Democratic (PSD) and Brazilian Labor (PTB) Parties, and by the illegal Communist Party - and Adhemar de Barros, leader of the Social Progressive Party (PSP) and Mayor of São Paulo. Quadros received approximately 48 percent of the vote; Lott about 32 percent; and de Barros, 20 percent.

For the Vice Presidency, the incumbent, João Goulart, president of the Brazilian Labor Party and candidate also of the PSD and the Communists, was returned to office over Milton Campos, the UDN candidate. In third position was Fernando Ferrari, a PTB dissident running as candidate of the PDC.

During the short period in which he occupied the Presidency, Quadros instituted a series of financial and economic reforms and indicated his intention of ultimately reforming Brazil's entire legal administrative and electoral structure. He also declared Brazil's foreign policy to be one of "independence" - a phrase which his detractors claimed was equivalent to neutralism but which his supporters asserted was a legitimate expression of Brazil's emergent great power status. This policy was distinguished by renewal of relations with various countries of the communist bloc, a drive for
closer relations with the emergent African nations and a clearly-enunciated policy of support of the Cuban regime of Fidel Castro.

President Quadros' sudden and generally unexpected resignation on August 25, 1961, threw the nation into the worst political crisis in its modern history. In his resignation "manifesto" Quadros asserted that he had been forced to resign by "reactionary" elements acting in concert with "foreign" (i.e., U.S.) influences. Many observers, however, believe that Quadros' resignation was one of a series of unsuccessful maneuvers designed to give him extraordinary powers, which would have included suppression of the Congress.

Congress accepted Quadros' resignation and installed Ranieri Mazzilli, President of the Chamber of Deputies (and No. 3 in line of constitutional succession) as acting President in view of the temporary absence from the country of Vice President Goulart. The Ministers of War, Navy and Army (backed by a considerable portion of the armed forces) soon announced their opposition to Goulart's accession to the presidency, and, at the same time, Goulart's brother-in-law, Leonel Brizzola, governor of Rio Grande do Sul, formed the so-called "Constitutionalist" movement, backed by the powerful Third Army and apparently prepared to fight for Goulart's installation as President. A compromise was subsequently reached, however, with the adoption of a parliamentary form of government (via constitutional amendment voted by the national congress with record speed) which considerably curtailed the powers of the presidency. The new government, composed of President Goulart and a Council of Ministers headed by Prime Minister Tancredo Neves, took office on September 3, 1961, subsequent to an overwhelming congressional vote of confidence. The new cabinet was a coalition supported by the Social Democratic, National Democratic Union, Christian Democratic and Social Progressive parties.

There followed a nine-month period of calm on the surface of domestic politics, while underneath convulsive fermentation was growing on the question of the merits of parliamentaryism vs. presidentialism. The first in a series of crises erupted in June 1962 when Premier Tancredo Neves and his entire cabinet resigned to comply with constitutional provisions forbidding candidates for public office to hold ministerial positions 90 days before elections. Several of the cabinet members wished to run in the October 7 general elections. President Goulart first named as the new Premier the then Foreign Minister, Dr. San Tiago Dantas (PTB), who was rejected by the conservative majority in Congress. The President then named the President of the Senate, Dr. Auro Moura Andrade (PSD), who was confirmed by the Congress but who resigned after the President declined to accept certain members of the Cabinet proposed by him. Finally, in August, the President proposed Dr. Francisco Brochado da Rocha (PTB) whom the Congress found acceptable.

Premier Brochado's tenure was stormy and short-lived, however. He resigned on September 14 because of his inability to obtain from Congress the special powers he regarded as necessary to solve the country's immediate problems and authorization for a plebiscite, to
be carried out simultaneously with the October 7 elections, to decide the issue of what form of government Brazil should have. (Brochado died of a heart attack a few days after resigning). On September 15 a bill was rushed through the Congress under which (1) the President was empowered to name a provisional Prime Minister and cabinet to function in the absence of a congressional quorum until such time as the Congress could accept or reject the Cabinet and (2) providing for a popular referendum to be held on January 6, 1963. It further provided that the Congress would have 90 days in which to act on the referendum decision should it call for a return to the presidential system. If it fails to act, the 1946 Constitution will again come fully into effect. On September 16, the President named Professor Hermes Lima (PTB) as the provisional Premier with the additional portfolio of Foreign Minister.

Thus, throughout the prolonged period of cabinet crises and of threatening rumors of impending coups from the right and from the left and of a situation in which governmental administration came to a virtual standstill, the Brazilian genius for political compromise prevailed. On October 7 in an atmosphere of almost total tranquility some eighty percent of 18.5 million registered voters went to the polls. They selected 409 Federal Deputies; 45 Senators (two-thirds of the Senate, plus three Senators for the new State of Acre); 11 State Governors (including Acre's) and 9 Vice Governors; 20 State Legislatures and one Constituent Assembly (Acre); and mayors and municipal councilmen in all or some of the municipalities in 17 states. At this writing (October 15) it is too early to assess the results in absolute terms, but it seems clear that the moderate political forces in Brazil are holding their own and that the new Congress is likely to be composed much on the same order as the present Congress.
Political Parties and Leaders

For the most part, Brazilian political parties are of recent foundation having been organized in 1945 and 1946 near the end of the Vargas dictatorship. They consequently have not yet acquired political traditions or developed long-run administrative programs, so that their organization and discipline are less tightly knit than is the case with United States parties. In many states there is little difference between the programs and electoral promises of the major parties, and electoral alliances based on temporary expediency are frequently made at state and local levels, even by normally antagonistic groups. A natural consequence of this system is that party discipline is relatively weak and there is a tendency toward more or less constant shifts of political figures from one party to another as well as recurring splits and factional disputes within each party. For example, on major legislation in the Congress, intra-party differences of opinion often result in voting which cuts across party line.

The present 326 members of the Federal Chamber of Deputies which will leave office on 15 March, 1963 represent twelve parties of which only four are of national significance. The classification of these deputies by parties is as follows:

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<td>PSD</td>
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The nationally significant parties are the following:

1. The Social Democratic Party (PSD) was founded in 1946 at the close of the Vargas dictatorship to contest the 1946 presidential elections. It was composed for the most part of Vargas supporters and was based on state and city political machines which had been created or continued during the Vargas Administration. The PSD is a right-of-center conservative party, with the country's strongest grass-roots organizational machinery and considerable financial support the former derived chiefly from long-time federal, state and municipal office holders and the latter from large business interests, principally in industry. Declining steadily in strength since its foundation, the PSD was almost utterly defeated in 1960, losing both the presidency and its long-time hegemony at the state and municipal levels. Ex-president Kubitschek, now a Senator from the state of Goiás, is unquestionably the party's most prestigious figure as well as its most outstanding leader.

2. The National Democratic Union (UDN) was formed in 1946 as a coalition of virtually all anti-Vargas forces, and, as such, functioned as the largest opposition party in Brazil until 1960. During the short-lived Quadros administration, the UDN was the largest party supporting the government. Like the PSD, it is basically right-of-center in its outlook, to which (as noted above - see "Political Events") it is allied in supporting, and participating in, the present government. The UDN now controls more state governments than any other
Brazilian party; in terms of congressional strength, it is the nation's second ranking party. The UDN's national president is Federal Deputy Herbert Levy. Its other prominent leaders are: Governor Magalhães Pinto of Minas Gerais, Governor Carlos Lacerda of Guanabara, Governor Cid Sampaio of Pernambuco and Governor Juraci Magalhães of Bahia.

3. The Brazilian Labor Party (PTB) was founded in 1945 by Getulio Vargas, principally as a means to secure mass working class support for his administration. In spite of its name, it has not so far developed into a left-of-center, labor-socialista party of the type found in England and the Scandinavian countries and, in the absence of a militant and well-organized trade union movement in Brazil, its principal leadership has been drawn for the most part from fairly well-to-do and basically conservative circles. However, with the growth of militant nationalism, leftist leaders are rising to positions of greater prominence within the party. Its National Chairman, João Goulart, is President of the Republic. The PTB, presently Brazil's third largest party, has grown steadily since its inception. Since the death of Vargas, Goulart has been unquestioned party boss.

4. The Social Progressive Party (PSP) was organized in 1946 by Adhemar de Barros, a Vargas lieutenant who had been appointed by the Federal Government to administer the State of São Paulo and who, after the fall of the Vargas dictatorship, ran for Governor in the 1947 election. With the Barros's victory, his personal political vehicles, the PSP, was able to consolidate its position and to broaden its base in the State of São Paulo. It has remained Barros's personal following and supported him unsuccessfully in the 1958 and 1960 presidential elections, but returned him to the governorship of São Paulo in the 1962 elections.

5. The Brazilian Communist Party (PCB) was declared illegal by the Federal Supreme Court in 1947, and has therefore been unable to present its own candidates for election to public office. However, as the most tightly organized and disciplined political organization in Brazil, the Communist Party, although forced to operate to a considerable extent clandestinely, is able to make its presence felt, especially in the propaganda field. The chief strength which the Communist Party has enjoyed in Brazil in recent years derives from its ability to identify itself with inherent nationalist feelings, and its principal effort has been to expand this growing nationalism and to turn it against the United States. With the reappearance of its leader Luiz Carlos Prestes, in March of 1958, the Communist Party embarked on a much more open course of action, ostentatiously proclaiming its intention to seek political power by peaceful and constitutional means and its readiness to cooperate with any political party or candidate prepared to endorse its ultra-nationalist program. This electoral gambit was not very successful in 1958 and 1962. Presently at one of its lowest levels of effectiveness due to factionalism and financial difficulties, the PCB, nonetheless, retains a voice in Congress and strong foothold in some regions.
6. The Small Parties. The smaller political parties are principally local or regional in character. Even those with a potentially nation-wide appeal (such as the Brazilian Socialist Party and the Christian Democratic Party) do not have sufficient strength to speak with significant authority at the national level.

Labor Movement

The modern labor movement of Brazil was created in 1937-1939 while Vargas was President. Today it contains an estimated three to four million adherents. There are five national confederations (Industrial, Commercial, Land transport, Credit institutions, River, Sea and Air transport) and a number of separate national and regional federations and local unions. The movement is financed largely by the deduction of one day's pay per year of each worker in the country; these sums are collected by the Government and distributed to the various unions, federations and confederations.

The three major national confederations are affiliated with the western, democratic ICFTU (International Confederation of Free Trade Unions). The Communists dominate one of confederations and some of the national and regional federations and local unions. Political parties, particularly the PTB (Brazilian Labor Party), exercise considerable influence in the labor movement.

The labor movement is steadily growing in size, experience and influence, although handicapped by lack of capable, experienced leadership.
REPORT TO THE PRESIDENT
BY THE
INTERDEPARTMENTAL
SURVEY GROUP ON BRAZIL

NOVEMBER 3, 1962

SECRET

Dear Mr. President:

In accordance with your wishes, the Secretary of State appointed us a survey group to visit Brazil and to submit appropriate recommendations. Our briefings in Washington started on October first; we spent ten days in Rio de Janeiro, a day in Brasilia, two days in Sao Paulo and three days in Northeast Brazil.

We learned that Brazil is on the verge of financial collapse. Since you then expected to visit Brazil in November, we dispatched preliminary reports on October 23 and October 25 to the Secretary of State. Although you have now postponed your Brazilian trip, we confirm our preliminary recommendations, and repeat them later in this report.

Scope of Our Discussions

Our discussions in Washington included meetings with most of those concerned with Brazil in the several departments of our government; and with the heads of the Export-Import Bank, the World Bank and the International Monetary Fund. In Brazil Ambassador Gordon and his entire Country Team in the cities we visited gave us every possible cooperation, advice and help. We talked there with many officers of all the U.S. agencies represented in Brazil.

One or more members of the group met with President Goulart, the Prime Minister, Finance Minister, Minister charged with Planning,

The President,
The White House,
Washington, D. C.
(Submitted through the Secretary of State)
Superintendent of Money and Credit (SUMOC) and with officials of the Banco do Brasil and of the Northeast Development Agency (SUDENE), as well as with several Governors, Military Commanders and other officials.

We met with groups from the American Chamber of Commerce in both Rio de Janeiro and Sao Paulo and with a number of other American and Brazilian businessmen and bankers. We had discussions with both the local and foreign heads of the two large utility companies, American Foreign Power and Brazilian Light and Power, which the Brazilian Government proposes to take over. In Panama, where we prepared much of this report, we had the benefit of the views of the Military Commander in the Caribbean area, whose interests include Brazil, and of his Political Advisor.

You will recognize that we could not check all the aspects of the problems involved in the time available and that our conclusions and recommendations, which are all unanimous, are necessarily largely based on a synthesis and analysis of the information and opinions given us by those with whom we talked.

THE COUNTRY TEAM

The United States is fortunate, in view of the critical financial and economic situation in Brazil, to have Ambassador Gordon with his broad economic and governmental experience as leader of the Country Team, a role he is successfully fulfilling. Indeed, it is through his high qualities of leadership, more than through normal institutional means, that the Country Team is made to function well. He is familiar with all policy directives from Washington and with the Country Team plans. His periodic consultations in Washington and his meetings with the Latin American Policy Committee there, have provided satisfactory coordination between the Washington agencies and the Country Team.

We find the quality of most U.S. officials in Brazil high and believe that they are functioning as a team and are generally pursuing the Country Team plans aggressively. The Ambassador and the Country Team generally enjoy a very high reputation among Brazilians and Americans alike. However, it must be recognized that no matter how competent the Country Team may be there are limits upon the power of the United States to control or even to influence the course of events in Brazil. Under the political and financial conditions existing at this time, we cannot expect our Country Team or its plans, no matter how carefully prepared, to be fully effective.

We make only one serious criticism of the Country Team operation and our criticism applies equally to Washington's inadequate staff support. We do not believe that the Alliance for Progress program in
the Northeast, to which the highest priority has been assigned, has been pursued with sufficient diligence or vigor. More will be said concerning this in another section.

Policy Guidance and Country Team Plans

In general, Washington policy guidance is adequate. Significantly absent, however, is any clear-cut expression of U.S. policy towards President Goulart stating precisely what should be done about him.

Country Team plans appear consistent with U.S. policy objectives and with lines of action recommended in "Guideline" papers and seem to be based on generally reliable intelligence.

One stated U.S. objective is to strengthen key Governors friendly to the United States by the use of economic assistance. It is unclear whether this implies that economic aid projects now foreseen in the Northeast Alliance for Progress program for the State of Pernambuco should now be withheld or substantially modified in magnitude or orientation, in view of the election of a pro-Communist unfriendly to the United States as Governor of that State. Clarification from Washington would be helpful, both in itself and as an indication of policy in similar cases.

Better communication facilities between Washington and Rio de Janeiro would do much to increase the speed of response to Washington's instructions, especially in emergencies. In the recent Cuban crisis your letter to the President of Brazil was delayed in transit to an extent which could have interfered with the accomplishment of your objective.

Intelligence

Various factors inherent in the Brazilian situation militate against the adequacy and reliability of the intelligence available to the Country Team as a basis for long-term planning. Aside from the normal limitations such as the availability of personnel, these include the geographical vastness of the country, its decentralized administration, its lack of good internal communications and reliable statistics, and the fluidity of the political situation.

Within these limitations, the availability of current intelligence, including military intelligence, is reasonably good and steadily improving. CAS is in a good position to cover Communist Party intentions and plans. The Country Team's total capability, both overt and covert, gives reasonable assurance of timely notice of any major impending development.
Contacts between members of the various U.S. agencies in Brazil and Brazilians are excellent in Brasilia and generally adequate in Rio de Janeiro and in cities where consular offices are established. Coverage diminishes in areas distant from these centers.

**Recommendation**

It is recommended that Washington issue clear policy guidance to our Mission in Brazil setting forth as specifically as possible our attitude, strategy and tactics towards the Goulart Administration. A suggested approach is contained in a later section of this report.

**THE IMAGE OF THE UNITED STATES**

There is in Brazil a long established and still effective tradition of special friendship with the United States, as between the two great, progressive, and non-Spanish powers of the Western Hemisphere. This tradition is still powerfully supported, especially within the military establishment, by pride in the fact that Brazil was the only Latin American state to make a substantial military contribution in World War II, as a loyal ally of the United States.

Since 1945 this favorable image has been clouded by a Brazilian feeling that the United States tends to take Brazil too much for granted, in particular that the United States has denied to Brazil the aid urgently required for its development while granting lavish aid to less important allies, and even to neutralists. This feeling that the United States has disregarded Brazil's needs and importance has been vigorously exploited by Communists and ultra-nationalists to whip up anti-American sentiment. These efforts have not materially affected the bulk of the population, but criticism of the United States and a sympathetic attitude toward Castro's Cuba have received increasing acceptance in political and intellectual circles.

The recent forceful action of the United States with respect to Cuba, and the revelation of the extent of the Soviet presence in that country, is doing much to restore a more favorable image of the United States in Brazil. The friends of the United States have been emboldened to speak up. Even such a violent critic of the United States as Brizola has now found it expedient to denounce Khrushchev's exploitation of Cuba in the face of the resurgence of pro-U.S. and anti-Castro sentiment.
THE POLITICAL SITUATION

The Brazilians are convinced that theirs is a great country with a great future and that they are competent to manage their own affairs. They are disposed to claim U.S. financial support as a matter of right in consideration of Brazil's importance to the United States, but are highly sensitive to any implication of U.S. tutelage or direction. This nationalistic attitude is not a new thing attributable to the perversity of the present Brazilian administration. It has been growing for a generation, but is now more acute than ever.

The parliamentary system which was improvised as a condition precedent to Goulart's accession to the presidency has failed to function. Since then Brazil has been virtually without an effective national government; all concerned have attempted to evade responsibility for the political drift and rapid financial deterioration which have characterized the period. Goulart has been obsessed with his struggle to recover full presidential powers.

The recent election was peaceful enough but it was not conclusive -- both left and right had gains and losses, and the presidential issue was not directly involved. Almost certainly, however, the presidential system will be restored through the plebiscite to be held in January.

Goulart's political career has been based on demagogic leadership of organized labor, after the fashion of Vargas and Peron. His future course is unpredictable. He is essentially a clever opportunist, with no strong motivation save his craving for popularity and personal power. He is facile in political maneuver, but plays by ear according to the need and inspiration of the moment. It is unlikely that he fully comprehends or is competent to cope with Brazil's desperate financial situation. He is not likely to take drastic remedial measures which would adversely affect his popularity so long as he can avoid them. If faced with a financial crisis which threatened his tenure of office, he would take whatever course seemed best calculated to ensure his retention of power and would have no personal conviction or inhibition against turning to the Soviet Bloc. The present deterrents to that course are (1) continuing hope of greater U.S. aid, (2) reduced Soviet prestige since the backdown in Cuba, and (3) fear of provoking a military coup.

A significant consequence of Goulart's political opportunism is the favor and patronage which he has shown to Communists and suspected Communists throughout his career, in return for their political support. Almost certainly Goulart believes that the men he has appointed to key positions in his administration are personally loyal to him,
but his tolerance and patronage have been affording the Communists an unprecedented opportunity to infiltrate the Federal bureaucracy.

The policy of the Communist Party in Brazil is calculated to make the most of this opportunity. The Party is numerically weak; it has no significant capabilities for revolutionary or guerrilla action. With the apparent sanction of Moscow, it has chosen to pursue its purposes by political action -- by identifying itself with and fomenting anti-U.S. nationalism and radicalism, by infiltrating the bureaucracy and the leftist political parties, by extending its influence and control in organized labor and student groups, and by working to regain legal status as a political party.

Traditionally, the Brazilian armed forces have considered themselves the guardians of constitutional order, above considerations of party politics. The unsuccessful attempt of the high command to prevent Goulart's succession spread confusion in the military establishment and weakened the unity essential to this traditional role. Goulart has now appointed to high command officers on whom he believes he can rely, because they share his political views, or because they are personally committed to uphold his constitutional authority. Although the bulk of the officer corps remains highly dissatisfied with the political tendencies of the Goulart regime, a military move to overthrow the regime is highly unlikely, except in the event of an extreme provocation or a severe national crisis.

In consequence, Goulart may well serve out the remaining three years of his term, unless the rapidly deteriorating financial situation and resulting popular discontent should become so acute that the military, with substantial political support, would conclude that a political change was imperative.

As long as Goulart remains in office, the United States should continue its efforts to make him realize the gravity of Brazil's financial and economic situation, and continue to urge the adoption of adequate remedial measures which would justify our large-scale financial help. At the same time we should attempt to influence his political orientation in directions better calculated to serve U.S. interests.

The United States should also intensify its intelligence concerning, and unobtrusively maintain contact with, any military and political elements of a potential and more friendly alternative regime, and should be prepared to act promptly and effectively in support of such a regime, in case the impending financial crisis or some other eventuality should result in the displacement of Goulart.

SECRET
same number of cruzeiros will now buy so much less. Some important manufacturing companies are already being forced to slow down their operations for this reason. Preliminary estimates of the 1962 expansion in gross national product indicate that it has been reduced by half to about 3 per cent and that it may be less than the population increase during this year. The situation is becoming more serious month by month.

Can the Inflation Be Stopped?

If the Brazilian Government determined that the well-being of Brazil depended upon taking the necessary drastic measures to curb the inflation, carefully explained the reasons for these to the Brazilian public and asked the support of the Armed Forces and of the public in such an all-out effort, it would and should have the powerful financial and moral support of the United States Government, the Export-Import Bank, the IMF, the World Bank and probably of several European governments.

There are many examples in postwar history of successful currency stabilization, followed by export growth, revived foreign investment and national prosperity. In France, four years ago, the foreign exchange reserves similarly almost ran out, but strong measures rigidly enforced soon instilled public confidence, replenished the country's foreign exchange and restored a balanced economy in a matter of months.

What is needed in Brazil, in the Government itself, in business circles and in the public consciousness, is the desire and the will-power to see a radical but necessary series of adjustments through the painful first year. Inflation in Brazil has become a way of life - many have found ways to live with it - the middle and poorer classes suffer most. Unfortunately, few in our Embassy or in Brazilian or American business circles believe President Goulart or his associates are willing to adopt and enforce the hard measures necessary to bring balance and prosperity back to Brazil.

The problem we face is to find a way to persuade President Goulart that this course of action is in the best interests of his country, and that only in this direction can he expect important financial support from us. If Brazil itself will make the effort and ample foreign help is made available, inflation can certainly be stopped over a reasonable period.
What Measures are Required?

The Brazilian technical people know perfectly well what is needed internally. The most important action required is to attack the budgetary problem and to make substantial progress toward a balanced budget by eliminating the huge subsidies to the railroads, the merchant marine, and the other state enterprises, and so making these services pay their own way; by cutting unnecessary and unproductive personnel and other expenses; by increasing tax rates and by improving tax collections. The Government will have to develop and firmly administer a proper wage policy. Strict controls on bank credit will be required, consistent with the degree of progress achieved in balancing the budget. Finally, more flexible and realistic foreign exchange rate and other policies must be adopted both to encourage exports and an inflow of capital, and to discourage unnecessary imports.

How Can the 1963 External Deficit be Handled?

In our preliminary report we gave a suggested illustration of the manner in which the huge residual deficit - in excess of $500 million - could be handled by postponing 1963 debt payments and marshaling all possible U.S., European and International Monetary Fund resources. Recent history indicates that the Europeans would not be willing to participate in a major way without International Monetary Fund participation. In view of the magnitude of the problem, we believe the operation is impracticable without the International Monetary Fund, but is feasible if the Fund participates fully. Since the attitude of the Europeans as well as private capital is heavily influenced by the IMF attitude, the availability of at least 200-250 million dollars probably hangs on the IMF decision.

On the other hand, IMF participation would be difficult to sell politically to the Brazilians. The IMF would undoubtedly insist on substantial prior performance by the Brazilian Government of measures which Brazilian officials would consider politically possible only on a gradual basis. This is the most difficult aspect of the entire problem, and there can be no assurance that the IMF and Brazilian positions can be reconciled.

Conclusion

Brazil is on the verge of financial collapse. While the internal inflation is extremely serious, it is the external obligations, which Brazil will soon be unable to meet without massive external assistance, which threaten international bankruptcy. The 1963 deficit
will reach almost one billion dollars. Even if an acceptable stabilization program were put in force by Brazil the magnitude of the deficit is such that the United States alone could not find the amount required. Only a consortium including the International Monetary Fund could bridge the gap. The IMF would undoubtedly insist on a Brazilian stabilization program which Brazil would consider harsh and politically impracticable. This is the dilemma.

**Recommendation for Immediate Action**

It is recommended that Ambassador Gordon be instructed to inform the Brazilian President and Finance Minister immediately of this assessment of the situation. He should then state that the United States is prepared to help if a viable solution can be found, explaining that U.S. resources alone would be insufficient even were an acceptable stabilization plan put in force. We suggest that he add that the resources of the European nations and Japan and the assistance of the IMF would all be needed and that it would be our considered and friendly suggestion that the Brazilian Government adopt an economic and financial program under standards which would be acceptable to those mentioned above. He could add that he feels sure the World Bank would be ready to finance large-scale new projects under these circumstances.

Time is very short since the Brazilian Constitution requires that tax legislation involving structural changes must be passed before November 30 (and even tax rate changes before December 31) this year if the legislation and the tax changes are to become effective in 1963. We therefore suggest that shortly after Ambassador Gordon's statement you personally confirm the United States offer of financial assistance along the above lines in a letter to President Goulart. Your confirmation of the fact that U.S. resources alone are insufficient to bridge the Brazilian balance of payments deficit may well be the only factor which might persuade President Goulart of this stark reality, and of the necessity for drastic action by his Government.

**Probable Future Developments**

While we consider it most important, politically and otherwise, that the above offer be made, and preferably in written form for possible later use, we consider it improbable that the Brazilian Government will accept this proposal or that the Brazilian Congress will actually enact the tax and other measures necessary to implement a stabilization plan satisfactory to the International Monetary Fund.
In this case, in the absence of emergency U.S. help, or of the large-scale debt postponement and important new financing which only an IMF approved plan would make possible, we do not believe that Brazil can avoid a default on its external obligations in the next few months, since so much of Brazil's three billion dollar debt is short term.

A general moratorium on external interest and principal payments would practically wipe out Brazil's external credit and place virtually all transactions on a cash basis. Even in this case, Brazil would probably make every effort to avoid default on IMF and World Bank obligations. Assuming the continued availability of PL 480 commodities and some loan commitments already made, the remaining deficit in the event of default could probably be managed for some months by cutting imports or other expenditures without extensive immediate damage to the economy. It is likely, however, that efforts will be made for some time to deal with the external payments problem short of default and without a comprehensive attack on the problem. Such a period might involve supply breakdowns and shortages severely disrupting the economy, affecting the everyday lives of the population, and leading to an acceleration of the inflation. A complete repudiation of the debt might defer this process for a short time but could not arrest it indefinitely.

It is hard to escape the conclusion that the developing financial crisis will soon begin to hurt seriously the general population and thus threaten the stability of the Goulart Administration. In this case, Goulart will certainly seek to transfer the blame from himself to the "hard-hearted Yankee imperialist bankers", and in this he would have the vociferous support of the Communists and ultra-nationalists. The likely result would be the final commitment of Goulart to the radical left, an intensification of anti-American sentiment, and the polarization of domestic political forces. In these circumstances, a military takeover might become the only alternative to a Cuba-type political evolution under Goulart or some successor.

These risks must be weighed in making the necessary financial decisions but we do not believe the high cost of postponing the crisis and buying time by U.S. aid alone is now justified nor long possible. Unfortunately, it would appear that conditions in Brazil must get worse before they can get better.

We do not wish to rule out the possibility of some limited U.S. help even on a balance of payments basis to avoid immediate default, provided it is clearly in the United States interest at the time and
that it allows more leeway for profitable negotiation between Brazil and the International Monetary Fund of a reasonable stabilization plan.

It should be clearly recognized, however, that any such action could only stave off a serious crisis for a very temporary period and any long postponement is both too costly and too difficult to defend.

If the United States decides to carry out the hard line we recommend, we urge that it be carried through to its logical conclusion and not changed in midstream as we understand has happened before in the face of the inevitable political and financial pressures which such a policy provokes.

The fact that Brazil supported the Cuban quarantine recently in the Organization of American States in no way alters our above recommendations, which are based on the practical financial possibilities as we see them.

Readiness for Additional Action

If the recommended approach by the Ambassador should meet a positive response from President Goulart and the proposed tax measure is approved in time by the Congress, the United States should bend every effort to assist in developing an adequate stabilization program in cooperation with the other creditor countries and the International Monetary Fund, all of whom we believe would take a constructive and helpful approach.

When and if the Brazilian Government repudiates or openly fails to meet its external obligations we suggest that the United States be prepared if then appropriate to make an immediate public announcement along the following lines.

a) The United States regrets the financial difficulties in Brazil which unfortunately are the inevitable result of the spiralling inflation during the past few years, coupled with policies which have discouraged and shut off the badly needed flow of new private investments to Brazil.

b) In spite of these inflationary and nationalistic policies the United States had constantly offered its help and several times had financed Brazilian stabilization plans which had never been carried through by the Brazilian Government.

c) In the last five years the United States including Export-
Import Bank loans and PL 480 food had made grants of ______ and loans of ______ and is now Brazil's largest creditor.

d) Nevertheless the United States is prepared to accept the Brazilian debt moratorium until such time as the situation warrants an appropriate new arrangement.

e) In the meantime, the United States is still willing to continue its help to Brazil while Brazil's internal and external economies are being brought into balance to avoid undue hardship on the Brazilian people. This help would include the basic commodities needed by Brazil, food and oil, by continuing PL 480 food for a total of 100 million dollars and by offering a new Export-Import Bank loan for, say, 50 million dollars to maintain the inflow of oil and so assure Brazil's food and energy requirements for a few months.

The statement suggested above would be designed to support the then existing government on a hand-to-mouth basis for a reasonable period while it adjusted to the shock of repudiation, and also to anticipate and offset the political repercussions from a possible offer of oil by Soviet Russia. Any additional aid from us, and its amount and composition, would depend on economic and political developments, and particularly on the attitude of the Brazilian Government toward the United States, and its ability to cope with its financial problems and to usefully employ our assistance. The appropriate use of our aid and other resources following the impending financial crisis could hopefully result in a stronger government better oriented toward the United States and better able to deal with Brazil's economic and financial problems. Such a government should have our full political and financial support.

ALIANCE FOR PROGRESS

In August 1961 the 20 American Republics established the Alliance for Progress to bring accelerated economic progress and broad social justice to their peoples. The United States promised financing, including long-term development loans, for this purpose, and the countries of Latin America including Brazil agreed to "devote a steadily increasing share of their own resources to economic and social development".

The United States has carried out its commitment by making available some $650 millions in funds of all categories. Unfortunately, however, as has been pointed out in this report, the Brazilian internal budget and external balance of payments were both
already badly unbalanced and the deficit in both has been steadily increasing ever since. Under these circumstances Brazil was in no position to carry out its agreement to devote additional resources to economic and social development. Its first priority task then, and one which is now an emergency requirement, was to try to save as much of the presently functioning economy and standard of living as possible.

The external deficit in 1963 will be close to a billion dollars but this large total includes an accumulation of unpaid bills and very large maturities because Brazil's external debt is on such a short-term basis. In round figures the Brazilian economy, judging from its unbalanced internal governmental budget and from its external deficit, (and after allowing for more reasonable debt repayment figures) has been consuming about a half billion dollars a year more than it has been producing. This is about 3% of the total Brazilian gross national product and is about half its annual expansion in recent years.

Until Brazil has found a way to balance its current overall external deficit by increasing exports, by reducing imports, by receiving foreign investments or foreign aid, by borrowing or by defaulting, or by a combination of these factors, it cannot effectively hope to carry out its agreements at Punta del Este on any substantial scale or to finance any other program for economic or social development which requires large additional resources.

More U.S. dollar grant or loan resources could of course be made available as an increased U.S. contribution to the Alliance for Progress. These could reduce the Brazilian foreign exchange deficit and their counterpart in local currency could be used to finance Alliance projects, if not required to reduce the internal budgetary deficit.

However, for us to urge the Brazilians under present conditions to contribute large amounts toward new Alliance projects from their own resources and so increase their internal budgetary deficit is not only unrealistic but also inconsistent with our own proper insistence that they balance their governmental budget and achieve internal financial stability.

In Brazil, Alliance for Progress accomplishments to date have not lived up to the "rising expectations" stimulated in the minds of many Brazilians by the widespread Alliance publicity. Moreover, the general opinion in Brazil is that the Alliance is only another name for the United States economic aid program, and that its outward manifestations are a few new housing, educational and water projects.
Actually, of course, the Declaration at Punta del Este went much further in defining the Alliance for Progress as "a vast effort to bring a better life to all the peoples of the Continent".

The many political, economic, agricultural, fiscal, educational, health and social objectives which were defined in the Charter make up a total and most worthy goal for the overall well-being of the people of any underdeveloped nation.

However, realization of most of these objectives is only possible in an atmosphere of political calm and financial stability. Any important accomplishments of the Alliance in Brazil on a scale which would perceptibly influence Brazilian economic and social life will have to await a solution of the present financial situation. Since the Charter was adopted in August last year, the successive political crises, the spiralling inflation and the nationalistic policies which have come into vogue have combined to circumvent its objectives.

We saw an Alliance housing project some twenty miles from Rio de Janeiro. It is one of the few Alliance projects nearing completion. In a few weeks four hundred families -- about two thousand people -- will move there from "favelas", the Brazilian name for local slums. It is a beginning, a good example, and terribly needed, but unfortunately will be like a cup of water thrown into the Amazon River. Eight hundred thousand poor people live in such slums in Rio de Janeiro alone. Aside from continuous migration from the hinterland, they increase at the rate of over three per cent annually or over twenty-four thousand a year. The new housing project, which takes over six months to complete, will house one month's natural increase in the slum population of Rio de Janeiro.

We must be more careful that our publicity and propaganda do not exaggerate the effect of Alliance projects on Brazil's daily life.

United States Aid for Northeast Brazil

The highest priority has been given to the Alliance for Progress program in Northeast Brazil. A Brazilian delegation headed by Celso Furtado proposed this program in meetings with you personally in July 1961. Ambassador Bohan and a team completed a master plan on January 30, 1962. The Bohan plan was accepted as an overall concept. After lengthy negotiations, a bi-lateral agreement was signed by the Secretary of State and the Brazilian Foreign Minister in April 1962, under which the United States agreed to make $131 million dollars
available for the first two years requirements, and Brazil agreed to contribute the equivalent of $1.6 million dollars.

Now, nearly seven months later, only $1.6 million of our promised participation -- or about 1% -- has been reduced to specific project agreements and the funds obligated, and less than $200,000 have actually been spent. This failure is the only serious criticism we have to make concerning the U.S. operation in Brazil, and we believe this criticism can justly be levelled at all those responsible in Washington, in Rio de Janeiro and in Recife.

There are many reasons for the delay, including top U.S. personnel changes and difficulties due to the Brazilian SUDENE staff's obstinate desire to almost completely control the program. An AID staff of 52 (originally set at 35) is now authorized for the Northeast area. AID Washington, despite heated cables from Ambassador Gordon and from Mr. Moscoso himself in August when visiting Brazil, has so far furnished very few of the experts needed. Only 20 are even now present in Recife, including original personnel and those loaned by our Rio de Janeiro headquarters. Unless the United States can do better than this in both staffing and in getting tangible results, we cannot hope through such programs to favorably influence either Brazilian living conditions or Brazilian attitudes toward the United States. We believe, contrary to the views of the Country Team, that the entire U.S. contribution of $131 million should and could be specifically obligated during the next six months, if sufficient high level pressure and priority are given to these projects by all concerned, and if red tape is not allowed to obstruct the operation.

There are still confused U.S. lines of responsibility as between Washington, Rio de Janeiro and Recife, and adequate communications are lacking between Rio and Recife. We suggest that these be resolved and the personnel shortage in Recife be corrected immediately. It would appear that the entire AID personnel procurement procedures in Washington need strengthening if the Recife situation is any indication of a general personnel deficiency. We also believe that much greater authority should be given Ambassador Gordon to approve individual projects within approved programs if the Northeast program is to achieve the necessary momentum.

Recommendation

It is recommended that the overriding need for financial stability be given precedence over the provision of additional Brazilian or U.S. funds for new Alliance for Progress projects except as counterpart funds become available which are not needed for budgetary support and can be used for this purpose.
It is further recommended that all presently approved Alliance for Progress programs, and particularly the Northeast program, be reduced to specific, funded projects just as rapidly as possible and in any case within six months, and then rapidly implemented, so that the planned impact on Brazilian economic and social life is not longer delayed. The Ambassador should be given ample authority to accomplish this.

THE POPULATION PROBLEM

The census figures in Brazil are only approximately accurate. The Government statistical agency reported the population as a little less than 71 million in 1960, the last census year. There have been various estimates of the Brazilian rate of population growth. The Population Reference Bureau of Washington, D.C., considered generally the most reliable agency in this field, estimated the Brazilian population on July 1, 1962 as a little more than 75 million, with an annual rate of increase during the past ten years of 3.4 per cent. This is the highest growth rate for any large country in the world. At this rate of increase Brazil’s population would double to 150 million people in 21 years, and to nearly 300 million by the end of this century. This would be a disaster indeed.

In our judgment, much of Brazil’s poverty and lack of progress, particularly in Northeast Brazil, is due to this extremely high rate of population growth.

Northeast Brazil includes nine States with a population in excess of 25 million, largely poverty-stricken, already overpopulated, and increasing annually by somewhere between 750,000 and 1,000,000.

The terms of reference provided to the Bohan Survey Team stated with reference to Northeast Brazil that "the economic and social structure is basically that of the last century; annual per capita income is equivalent to only about $100...conditions are most depressed and prospects for improvement appear least promising in the arid interior of the region. Poor land, low productivity and living standards, and disastrous droughts have forced some migration, but not nearly enough to counter-balance the high birth rate and steadily rising population. Thus, the standard of living has continued to decline". The Bohan Team, after several months of investigation, came to this same conclusion, reporting that "because of this population pressure, the overall economic condition continues to deteriorate".
This is one of the areas to which you undoubtedly referred in your 1961 Message on Foreign Aid, when you said, "The magnitude of the problem is staggering. In Latin America, for example, population growth is already threatening to outpace economic growth -- and in some parts of the continent, living standards are actually declining." Since you said this a year and a half ago, the population of Brazil has risen by nearly four million persons.

Our own group has never seen worse slums than in the northeast Brazilian city of Recife, with a population of 800,000. Conditions in the dry interior were said to be even worse. This is borne out by the fact that continuing migration into Recife, along with normal growth, is increasing its population, according to sources in that city, by nearly 20 percent a year. The only panacea suggested by either the Bohan Report or SUDENE for the problem posed by the rising population and the resulting deterioration, has been emigration to other areas.

The present Northeast area is admittedly overpopulated. The impossibility of successfully resettling the annual increase in population, which will soon exceed one million each year, seems self-evident.

U.S. agronomists in the area advised us that large-scale surveys and agricultural land-use studies must precede any useful large-scale resettlement program, and that the numbers that could be resettled under any conceivable circumstances would be far less than the present population increase.

It is of course important to increase agricultural and industrial production as rapidly as possible, and to resettle people in other areas where feasible. However, unless the present rate of population increase can be greatly reduced, we are convinced that conditions will get steadily worse in Northeast Brazil, despite the SUDENE or Alliance for Progress plans.

Unfortunately, many Brazilians do not recognize this fact. They say there is so much land in Brazil that they see little or no objection to the present rapid growth of population. They do not seem to understand the magnitude of the problem, or the difficulty and high cost of large-scale resettlement programs.

Brazil is, of course, not the only nation which has been facing rapid population growth. In Japan, the serious nature of the problem was recognized shortly after World War II and in recent years the
birth rate has been dropping more rapidly than the death rate. India, Pakistan and Egypt have recognized the need for population control. The fact that Brazil is a Catholic country obviously makes the problem more difficult, although Puerto Rico has shown that intelligent leadership can deal with this problem even where the population is largely of this faith.

Actually, the Catholic and non-Catholic positions are not as far apart as has been commonly supposed. Pope Pius XII stated more than ten years ago that "we affirm the legitimacy and at the same time the limits -- in truth very wide -- of a regulation of offspring". The Pope expressed the hope that scientific research would succeed in giving the licit or rhythm method of birth control a sufficiently secure base.

Of course birth control should not be imposed on anyone. Each individual, each religion and each country should apply only those controls considered admissible by existing religious or national customs, and by the conscience of the individual. But the population explosion threatens the well-being of many areas of the world, as we have so graphically seen in Northeast Brazil, and calls desperately for some sensible solution.

We believe that the time has come for the United States to consider and if possible adopt a clear-cut and carefully thought through policy which recognizes the relationship between rapid population growth and economic development, and the consequent impact on United States aid programs. The U.S. policy should provide, in our judgment, for concentrated demographic and medical research and for appropriate assistance to countries requesting help in this important area. However, we believe the subject requires concentrated study and discussion by those best qualified in this field in order to arrive at a sound national policy.

Recommendation

We recommend that you appoint a Commission to study the implications of rapidly growing populations and their relationship to economic development, particularly in underdeveloped countries, and to recommend to you the related policies best suited to accomplish the aims of the United States in its foreign economic assistance programs. Such a Commission could usefully include not only representatives of the interested U.S. Government departments such as State, AID and HEW, but also top level demographers, medical authorities, sociologists and representatives of the religious groups interested in this problem.
OTHER ECONOMIC PROBLEMS

During the past two years Brazil has pursued illogical and wasteful policies in a number of economic areas. These policies have been largely motivated by nationalistic and at times anti-American considerations.

One of the worst of these economic mistakes has been the President's decision to take over all telephone, electricity and gas companies. The private companies involved are quite ready to sell since inadequate rates under government regulation have prevented their earnings from keeping pace with the inflation, and therefore from providing the needed expansion of their services. The takeover will, however, involve the addition of about one billion dollars to the Brazilian Government's internal debt, assuming it makes a fair settlement. This will also add large interest and principal payments to Brazil's annual internal budget and to its external balance of payments, even if 75% of the amounts received by the companies are reinvested in Brazil, as the government proposes. Perhaps an even more serious consideration is the responsibility which the Government will assume to provide efficient management and technical direction of the utility companies, and to finance the necessary large annual expansion of these services. It will also open these industries to possible corruption. If insufficient rates are charged, as is often the case with government-owned utility companies, annual large scale government subsidies will be required.

Although Brazil has enormous deposits of high grade iron and manganese ores, repeated obstacles have been thrown in the way of their national exploitation by foreign companies holding concessions. Potential exports of perhaps as much as 100 million dollars a year have been lost through this policy of obstruction.

In the field of oil, nationalistic opposition has prevented the expenditure of many million dollars by American oil companies for exploration. Whether the use of American resources and know-how would have resulted in the discovery of great amounts of oil we cannot know. However, oil imports now cost Brazil some 250 million dollars a year, and a sensible economic policy, unclouded by nationalism, would certainly have sought outside help in solving Brazil's large and important petroleum energy problem.

During the current year a very unfavorable and much discussed law regulating the remittance of profits by foreign investors was enacted. There is a possibility that some of the worst features of the new legislation will be repealed under a bill now under consideration by the Congress, but its psychological effect on foreign companies in Brazil has been extremely bad.
The above factors, together with the existing political and financial difficulties and uncertainties, have practically stopped the flow of foreign private capital to Brazil.

In the agricultural field coffee still accounts for two-thirds of Brazil's exports in spite of recent efforts at diversification. Although there is a severe shortage of foreign exchange, we found no great pressure by governmental officials or businessmen to find ways and means to increase Brazilian exports. We were told by those in a position to know that the internal price of meat and cotton is higher than the export prices and therefore they prefer to sell these products in Brazil rather than in the export market. We were informed that both meat and cotton, and sugar as well, could be sold abroad in very much larger volume if the government adopted realistic exchange rate and other policies designed to encourage export. It may also be true that encouragement for export would find foreign markets for Brazilian automobiles and other machinery, since Brazil has made far more progress in producing articles of this kind than has any other Latin American country.

Brazil imports nearly 200 million dollars worth of wheat a year. About one-half of this is supplied by the United States under Public Law 480 without foreign exchange cost to Brazil. Imports of PL 480 wheat have been steadily growing. The remaining wheat imports are bought from Argentina and Russia, or are imported from the United States against payment in sugar.

During the past five years Brazilian wheat production has gone down from more than 600 thousand tons a year to less than 200 thousand tons in 1962, even though Brazil's wheat requirements in the meantime have risen to well over two million tons.

It is obvious that the internal wheat price paid to the producer in Brazil has been unattractive, so that a great many wheat areas have been switched to rice and other crops. The internal price structure for wheat and flour have undoubtedly been influenced by the availability of "free" PL 480 wheat and the natural desire to keep bread prices low. However since PL 480 wheat will not be available indefinitely to Brazil, we should couple our continuing cooperation under PL 480 with technical assistance to the Brazilian agricultural planning agencies so that Brazil will again increase its internal wheat production. Otherwise Brazil will face a serious and increasing need for foreign exchange to pay for large scale wheat imports when PL 480 wheat is no longer available.
Recommendation

It is recommended that our Mission do everything possible to persuade the Brazilian Government of the importance of increasing its exports of both agricultural commodities and industrial goods, and of adopting realistic exchange rate and other policies toward this end.

Our Mission in Brazil should also offer its cooperation and technical assistance to help Brazil increase its internal wheat production, to avoid the serious and increasing need for foreign exchange for wheat imports when PL 480 wheat is no longer available.

THE MILITARY ASSISTANCE PROGRAM

This program is proceeding normally. It is primarily concerned with strengthening internal security in Brazil and with replacing engineering equipment to permit increased civil works by Army units (roads, railroads, dams, municipal water systems, etc.) as an aid to the Brazilian economy. Civil works programs contributing to the social and economic life of the country were traditional in the Brazilian military long before there was any U.S. assistance. This is one reason for the respect and trust with which the Brazilian people regard their military forces.

It is generally accepted that the Brazilian military establishment is the nation's most consistent anti-Communist and pro-U.S. element. The Army particularly enjoys a high reputation as guardian of the Constitution and of public order, and is the most effective single force standing for stability in the country.

This orientation is being undermined by recent actions of President Goulart in appointing several leftist or anti-U.S. officers to high command, replacing officers (anti-Goulart or pro-American) who had opposed or might oppose his policy. Unfortunately, one of these anti-American officers commands the Army in the area of Rio de Janeiro, which contains most of the units supported by the U.S. Military Assistance Program and considered to be the best in the Army.

One of the strongest links between Brazil and the United States was forged during World War II when the Brazilian Division participated in the Italian Campaign. Since then this comradeship has been fostered by training many Brazilian officers at military schools in the United States. During the past two years only a small percentage of the officers offered training in the United States have been permitted to accept, although recently more officers are being given such assignments. Financial difficulties have been cited as the reason.
but it is believed that anti-American influences are also at work. To correct this situation, we should urge the Brazilians to use vacancies offered to them, and make available as many more as they will accept.

A serious rift has developed between the Brazilian Navy and the Brazilian Air Force. An aircraft carrier was bought from Britain. The United States furnished planes and training to Brazilian Air Force pilots, for use on the carrier, but the Brazilian Navy has never allowed them on board the carrier. Apparently with help from our Navy, the Brazilian Navy has had its own pilots trained in the United States and has both openly and surreptitiously tried to obtain planes in the United States for use on the carrier. This dispute is still unresolved. At the earliest appropriate time, the United States should bring pressure on the two Services to resolve this controversy, with clear indications that military aid would otherwise be withheld from both Services.

THE INFORMATION PROGRAM

Information support of the Alliance for Progress program is the priority activity of the United States Information Service in Brazil. Publicity plans are well conceived and coordinated, and then carried out on a multi-media basis. Good working relations with the press and other media facilitate the placement of the large output of USIS prepared media material. A poll in Brazil indicates that over half of the people queried have some knowledge of the program of the Alliance. In an endeavor to correct a widely prevailing Brazilian impression that the Alliance for Progress is simply a new name for USAID programs, USIS is generating publicity emphasizing the Brazilian role in the Alliance for Progress.

During the financial difficulties that are threatening the Brazilian Government, it will have little opportunity to push the projects of the Alliance for Progress, and therefore our publicity should be played in low key. This is important since unfriendly politicians have built up considerable anti-American sentiment by attacks on exaggerated accounts of Alliance accomplishments.

A second objective is designed to encourage and strengthen the democratic center in its determination to withstand Communist influence and to resist encroachment by either extreme right or left wing influence. This program could be usefully expanded through increasing the publication of appropriate pamphlets and booklets, speeding up the production of low-priced books, circulating anti-Communist exhibits and increasing support to the bi-national centers in underprivileged neighborhoods.
Cultural Program

The cultural program, substantial in size and scope, is successfully reaching target audiences. The program appears to be well-planned and effectively carried out. Contacts with cultural groups, although extensive, need to be broadened out, particularly among the universities.

The increasing Communist influence among university students and labor groups presents a psychological problem making desirable the development of a coordinated special project of major proportions using the facilities at the command of USAID as well as USIS to build and staff Student Unions at the major universities; to create chairs of American History and American Literature; to present representative collections of American reference and text books to University libraries and to labor organizations; to support a program of cultural and athletic events under the President's Fund Program; and to expand the exchange of students and labor leaders to twice its present size.

SUMMARIZED RECOMMENDATIONS

Political

Washington should issue clear policy guidance setting forth the United States attitude, strategy and tactics toward the Goulart Administration.

Financial

Ambassador Gordon should immediately inform President Goulart of the U.S. assessment of the Brazilian financial situation, should explain that the size of the 1963 external deficit is too large for U.S. resources alone to meet, should nevertheless offer our help, if a workable stabilization plan is made effective, and should recommend that Brazil adopt a stabilization plan acceptable to the European creditors and to the International Monetary Fund, whose help will also be required.

We suggest that you confirm this position and offer of help in a personal letter to President Goulart for the record and for possible future use.

Because the Brazilian Constitution requires that legislation making structural tax changes be enacted before November 30, 1962 and making changes in tax rates before December 31, 1962, if the legislation is to become effective during 1963, we believe these recommended actions
should be taken at the earliest possible moment.

If the Goulart Administration accepts these suggestions, and the Brazilian Congress enacts the necessary tax legislation, the United States should do everything possible to negotiate a stabilization plan acceptable to the Brazilian Government and to the International Monetary Fund.

If, however, no satisfactory plan is worked out and the Brazilian Government is unable to meet its maturing obligations, the United States should still offer limited help, such as PL 480 wheat and an Export-Import loan for oil, while the Brazilian situation is being clarified, attempting to use aid and other U.S. resources to orient the Brazilian Government as closely as possible toward U.S. objectives.

Alliance for Progress

The overriding need for financial stability in Brazil should be given precedence over new Alliance for Progress projects, except as counterpart funds become available which are not needed for budgetary support.

All presently approved Alliance for Progress programs, and particularly the Northeast Program, should be reduced to specific, funded projects within the next six months and implemented as rapidly as possible. The Ambassador should be given ample authority to accomplish this.

Population

We recommend that you appoint a Commission to study the implications of rapidly growing populations and their relationship to economic development, particularly in underdeveloped countries, and to recommend to you the related policies best suited to accomplish the aims of the United States in its foreign economic assistance programs.

Economic

The United States should stress the need for increased Brazilian exports of both agricultural commodities and industrial goods, and should encourage Brazil to increase its production of wheat to reduce its future dependence on PL 480 wheat from the United States.

Military

Every effort should be made to increase the number of Brazilian officers assigned for training in U.S. Military Schools, as only a
small percentage of available vacancies have been filled during the past two years.

Our Mission in Brazil should bring pressure at the earliest appropriate time on the Brazilian Navy and the Brazilian Air Force to resolve the controversy that now makes the only Brazilian aircraft carrier inoperable and which has caused a serious rift between these two services.

CONCLUSION

The political and economic future of Brazil is of tremendous importance to the United States. Its orientation toward or away from the West will greatly influence the other Latin American Republics.

While the present difficulties in Brazil are primarily financial, they stem from what we believe is an incorrect economic philosophy.

Brazil has given the expansion of her economy highest priority among her economic objectives, and has counted on inflationary governmental spending and United States aid to make up any resulting deficit. Nationalistic policies have put up bars to the vital capital from abroad that otherwise would have eased Brazil's problems.

Economic laws eventually operate in the same way throughout the world. Brazil is no exception to the fact that a depreciating currency robs the population generally of its savings and that inflation, if uncontrolled, eventually leads to financial disaster.

Germany and Japan are examples of war shattered economies which adopted sound measures to rebuild their currencies and to restore their prosperity. In both countries the spirit of the slogan "Export or Die" became the dominant force that led to the solution of their balance of payments difficulties, which were much greater in 1945 than Brazil's similar difficulties are today.

France, Greece and Spain are other examples of countries which have overcome their internal budgetary difficulties and their external deficits by adopting sound but harsh measures and then strictly enforced them.

Political calm and economic sanity are both essential to solve Brazil's difficulties.

In Germany, Adenauer and Erhard have made up the politico-economic team. In Japan it was Yoshida and Ikeda. In France General de Gaulle held the fort while Pinay carried out the economic program.
If we could persuade President Goulart of this thesis - this economic philosophy - and he could keep Brazil calm politically while some man of his choosing laid down and enforced the necessary financial and economic measures, Goulart could become the saviour of his country's economy.

Perhaps this is too much to expect or even to hope for, but as the traditional and sincere friend of Brazil, and in our own interest as well, we should do our utmost in this direction.

Respectfully yours,

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