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SUBJECT - FY 1969 Program Submissions - Major Issues

- REFERENCE -
- 1) CA-5426, January 21, 1967
 - 2) AIDTO Circ. XA 2031, February 28, 1967
 - 3) AIDTO Circ. IA 135, March 1, 1967

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JOINT AID/STATE MESSAGE FOR AMBASSADOR AND AID MISSION DIRECTOR

This message supplements world and region-wide guidance already provided in referenced circular ~~airgram~~ airgrams. It should assist the USAID and Country Team in the drafting of the Economic/Social sections of the Country Analysis and Strategy Paper (CASP) and of the more detailed aggregate and sector strategies in the AID Program Memorandum.

USAID

170p

The 1966 Program Memorandum for Brazil met a very favorable reception in Washington. Its broad analytical framework for U.S. assistance strategy forms the basis for our FY 1968 Program submission to the Congress, and has provided a sound justification for continued allocation of a large proportion of total Alliance funds to Brazil. Nonetheless, a number of unresolved issues arose during the fall program review and during discussions of the proposed FY 1967 Program Loan. These issues, together with questions stimulated by the change of administrations in Brazil, and by a greater need in Washington for comprehensive sector strategies, should condition this year's submissions.

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Brazil's long-range development planning efforts have moved substantially forward in the past twelve months. A new government will soon be taking office with perhaps somewhat different development priorities and attitudes toward U.S. assistance. The USAID now has the benefit of several research studies which should help illuminate issues that were poorly understood in early 1966, and it can also better test certain Program Memorandum assumptions against

PAGE	PAGES
1	OF 8

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CLASSIFICATION

AIRGRAM

Department of State

AIRGRAM

CONTINUATION

POST	AID TO CIRCULAR XA	NO.	SECURITY CLASSIFICATION	PAGE	PAGES
AMEMBASSY, RIO DE JANEIRO	AMEMBASSY, RIO DE JANEIRO		CONFIDENTIAL	2 OF	8

Brazilian institutional capabilities. Also we have found from a year's experience with the Program Memorandum that analysis can best take place through asking at both the aggregate and sector levels what are the principal changes or reforms desired in the Brazilian economy, institutions and public policy and how can we best use aid both as leverage to get these reforms and to transfer real resources to help implement them. For these reasons, AID/W looks forward to an even higher standard of analysis in the 1967 program submissions from Brazil.

Listed below are some of the issues concerning our development assistance strategy for Brazil which are likely to arise during Washington or field program reviews this year. We welcome informal, frank exchanges with the Mission on these or other questions during the coming weeks to insure the best possible preparation for the Washington IRG reviews of the CASP and the field review of the draft Program Memorandum scheduled for August.

A. General Policy Issues and Macroeconomic Strategy

1. To what extent are GOB objectives and intentions consistent with the development goals stated in the 1966 Program Memorandum? To what extent are we describing only U.S. hopes for Brazil and to what extent are they Brazilian goals which the new government will actually pursue? The answer to this should more clearly reveal the degree of change to be sought and the leverage necessary to bring this change about. Two particular points require treatment.

- a) The nature and likely influence of government planning (macro, regional, or Sectoral) over the next four years. Is Brazil likely to swing back toward more decentralized decision-making by various government agencies on economic policy issues? If so, what changes are necessary in our analytical approach, or in our assistance program? (e.g., Univ. Calif. contract)

At the present stage of national planning in Brazil, what is the Mission's judgment as to the overall viability of the resource allocations projected? Are they politically feasible, and economically sound?

- b) Given ~~the political~~ outlook for the new government described in Embtel 8620 What are the likely parameters of U.S. influence in bringing about the changes identified under (1)? Can the extensive U.S. influence on GOB decision-making, particularly in sensitive domestic areas such as national, development planning, monetary policy, tax administration, education reform, etc. be sustained during the next administration? Will the political climate require alteration or abandonment of the program loan negotiating procedure developed so successfully with the Castello Branco Government? How can broad self-help commitments best be elicited under Costa e Silva? How could putting all lending on a project or sector basis within two-three years affect U.S. leverage? (Note that to date we have been singularly unsuccessful in exerting leverage on this basis in other Latin American countries).

SECURITY CLASSIFICATION
CONFIDENTIAL

DEPARTMENT OF STATE

AIRGRAM

CONTINUATION

POST	NO.	CLASSIFICATION	PAGE	PAGES
AIDTO CIRCULAR XA		CONFIDENTIAL	3	OF 8

2. Does the total impact of U.S. assistance programs in Brazil tend largely to bolster the status quo; identify the U.S. with modernizing trends in Brazilian society, both economic and political; or have neither effect in any clear way? Are Alliance for Progress programs affecting the internal power structure in Brazil to any appreciable extent? (possible examples: political effects of coffee diversification program if any; lagging agrarian reform efforts of GOB; education reform efforts and their effects on politically active students, etc.) Do U.S. programs have any discernible effect toward reducing regional disparities, or towards increasing popular participation in the development process?
3. Macroeconomic issues within the 1966 Program Memorandum model:
- a.) Are there any changes in the employment assumptions of the Program Memorandum? What are the most recent data on employment trends, growth of labor force (rural and urban), and best current estimates for investment/job ratios in both urban and rural sectors?
- b.) What are the real development effects of the proposed degree of import liberalization? Is the resource transfer of investment goods now taking place more effective than previously? What are current import coefficients for new investment in selected areas? Are the import projections in the 1966 PM still valid? What further liberalization measures are needed? What implications should be drawn from the Clark study? Is the level of projected foreign exchange reserves reasonable? Does Brazil's foreign exchange position suggest a lesser requirement for balance of payments support and a consequent shift in 1968, 1969, and beyond to sector and project loans?
- c.) What are the best current estimates of payments flows from exports, other lenders, and from private foreign investment? For planning purposes, ~~xxxxxx~~ assume ~~xxxxxx~~ prices will rise above present levels ~~xxxxxx~~ that coffee prices will remain at present levels.
- d.) How can the actual allocation of U.S. assistance be shifted more rapidly to reflect the sectoral priorities described in the 1966 Program Memorandum?

The major share of U.S. resources from project lending continues to go into power, industry and transportation. While appreciating the importance of road construction/maintenance and agro-industrial development to agriculture, how can a more rapid shift away from other types of infrastructure lending be achieved? In considering this question the Mission should discuss factors which may now limit the transfer of U.S. resources to priority sectors such as agriculture and education, e.g., restrictions on local cost financing, concern for U.S. export promotion, institutional weaknesses, etc. We expect the Mission throughout the Program Memorandum to present what it considers to be the optimum development strategy, clearly pointing out the costs to this strategy should other policy choices, e.g., reduced local cost financing, be selected. In the selection of projects for U.S. financing consideration should be given to the ~~xxxx~~ relative cost of procurement from the U.S. and from other sources.

CONFIDENTIAL

CLASSIFICATION

PROGRAM
CONTINUATION

POST	NO.	CLASSIFICATION	PAGE	PAGES
AIDTO CIRCULAR XA MEMORANDUM TO THE DIRECTOR		CONFIDENTIAL	5 OF	7 8

- c) Can savings and foreign investment really increase at an adequately rate to allow an 8% growth rate and a politically tolerable increase in ~~consumption~~ consumption?

From 1939 to 1960 national income in Brazil grew by about 229% with the ratio of savings to gross domestic product remaining relatively constant. Leff indicates that this was largely based on heavy foreign investment and short-term supplier credits and resulted in a redistribution ~~of~~ of income such as to substantially increase consumption. With the development of such consumption patterns (and the resulting political consequences likely from continuing austerity at the level of 1966) plus the increasing defensiveness in key sectors of Brazilian industry in the face of outside penetration, how can the pattern of growth be reoriented to provide for a greater degree of savings but also permitting a consumption level which is politically tolerable? While such a pattern does require, we think, a substantial inflow of private foreign capital what policies would maximize the inflow that is politically tolerable to the Brazilian business community and the new government? What would be the implications for the stabilization program of policies which would permit such growth?

Given the above analysis, what alternatives to the Program Memorandum model are most likely?

Sector Issues

The sector discussions should to the extent possible present a comprehensive strategy for agriculture, and education, and a general plan of action for public administration. They should proceed from the question of reforms or changes needed and proceed to the A.I.D. leverage to bring such changes ~~about~~ about. They should state wherever possible how far Brazilian society has moved during the last 12 months toward the quantified targets in last year's Program Memorandum.

1. Agriculture: The agriculture sector paper should provide a comprehensive strategy to integrate the total U.S. program in the sector. For example, changes in credit policy and total credit requirements should be so stated to permit comprehensive ~~analysis~~ analysis of counterpart requirements for this purpose from the Program Loan, the Sector Loan, and the P.L. 480 agreement. Some important questions are:
 - a) Will the presently planned coffee diversification incentives be sufficient to bring supply into ~~balance~~ balance or will additional policy changes be required?
 - b) Is there real economic justification for the GOB's channeling more credit to the agricultural sector for export promotion or for employment creation? If so, how much more? Should credit be concentrated in a few regions where it promises greatest returns?
 - c) What have been the ~~real~~ real effects of pricing policy changes in ^{SUGAR} non-coffee ~~agriculture~~ agriculture on real return to the farmer, and what additional changes, if any, should the U.S. seek?
 - d) What is the present state of improving the operations of the Ministry of Agriculture, of clarifying responsibilities and simplifying procedures? How may AID best further a more rational coordination of the numerous extension, research, ^(WORKER USINEIRO/FORNECEDOR)

CONTINUATION

POST	NO.	CLASSIFICATION	PAGE	PAGES
AIDTO CIRCULAR XA	2197	CONFIDENTIAL	8 OF	8

- b) How soon can we reasonably expect reliable and timely data on the national accounts, on the labor force and on unemployment? What progress is being made to improve statistics in such fields as agriculture, domestic commerce, industry, demography, etc. and what is/should be offered by outside donors?
6. Project and Sector Lending: In relation to the development loans proposed, the P.M. should summarize for both sector and project lending, the contingencies involved and the general target dates for authorization.

The purpose of the Program Memorandum is to summarize program recommendations concentrating on the principal issues and choices we face in FY 1968 and FY 1969. Treatment of many of the issues listed above should appear in one form or another in the CASP and the draft Program Memorandum; others are merely suggestive as to kinds of analysis whose results would strengthen this year's Program Submission from Brazil if they can be undertaken. Some questions probably cannot be answered, and a frank recognition of that fact is useful. The Mission can pose a greater ~~xxx~~ many more issues, for those listed here merely illustrate the kinds of problems raised by an assistance program this large and complex. To the extent that they can be addressed in the draft P.M., however, AID/W will be better equipped to review constructively the Brazil submissions.

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