

9 October 1964

MEMORANDUM FOR THE DIRECTOR

SUBJECT: Problems Confronting the Frei
Administration in Chile*

SUMMARY

Frei's impressive popular majority reflects not only a present reaction against Castro-Communism, but also the popular expectation that he will accomplish a radical economic and social transformation of Chile, with US aid, in keeping with the Alliance for Progress. To succeed in that, he must overcome formidable economic problems. As an essential first step, he must reach agreement with the Anaconda and Kennecott copper companies. He is willing to assure them against nationalization, but must obtain sufficient "Chileanization" of the Chilean copper industry to enable him to represent that Chilean sovereignty has been asserted.

Frei's efforts to achieve long overdue reforms in Chile by constitutional means will be closely watched throughout Latin America. If he succeeds, with US cooperation and support, the Alliance for Progress will be greatly strengthened. If he fails, his failure would lend support to Fidel Castro's thesis that real reform can be accomplished only by violent revolution.

* This memorandum was prepared in consultation with DDP, OCI, and ORR.

1. The election of Eduardo Frei to the presidency of Chile was a stunning defeat for Castro-Communism, but does not in itself ensure the elimination of that danger. Frei's impressive popular majority reflects not only a present reaction against Castro-Communism, but also a popular expectation that Frei will accomplish a radical economic and social transformation of Chile, with US aid, in keeping with the Alliance for Progress. Frei is fully committed to that endeavor, but to succeed he must overcome formidable obstacles. If he should fail, the consequent popular disillusionment would almost certainly produce a further growth of the extreme left and might bring a Communist-Socialist combination to power in the 1970 presidential election.

2. Chile's human and material resources are adequate to provide a decent living for its rapidly growing population, but only if more rationally utilized, with a more equitable distribution of the national income. For years the economy has been virtually stagnant. It is vitally dependent on the export earnings of a copper mining industry dominated by two US firms, Anaconda and Kennecott.* As a result of prolonged neglect of agricultural development and the under-utilization of land, Chile must now import foodstuffs which it formerly exported. Manufacturing industry, fostered by protectionist

* The copper mining industry now provides nearly 90 percent of Chile's export earnings and 15 percent of its tax revenue.

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policies, is also inefficient and still a drain on export earnings. Servicing an external debt of \$1.4 billion imposes a further heavy burden on the country's balance of payments at a time when new investment is urgently needed in such basic development areas as transportation, communications, electric power, housing, and education.* For years Chile has suffered from foreign exchange and budgetary deficits, both of which increase pressures for raising taxes on copper, Chile's one profitable resource, and from an inflation which, during the past two years, was at a rate of 50 percent per annum. Underemployment is chronic; the real income of most of the population has declined.

3. As a first step toward coping with these problems, Frei is seeking to persuade the US copper companies to make the substantial new investment needed to increase copper productions for export. Those companies have been unwilling to make new investments in Chile unless given reliable assurances against nationalization or confiscatory taxation. During the election campaign Frei countered his opponent's demand for nationalization by proposing "Chileanization." This term has not been defined. It appears to mean sufficient Chilean control to ensure an increase in production, much more

* During the past two years US program loans have financed nearly 40 percent of Chilean public investment in these areas.

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refining of Chilean ore in Chile, and some voice in the marketing of Chilean copper. Frei is willing to give the desired assurances and to negotiate on the subject of tax adjustments. In anticipation of Communist charges of a sellout to the Yankees, it is politically imperative for him to obtain in return a sufficient degree of "Chileanization" to enable him to claim that Chile's national sovereignty has been asserted.

4. An agreement with the copper companies on these lines would increase Chilean foreign exchange earnings and tax revenue. Frei would also expect it to facilitate the financial arrangements needed to cope with residual foreign exchange and budgetary problems pending the more even development of the Chilean economy. In particular, he hopes to negotiate a reduction of debt service requirements from \$290 million a year to \$120 million, which he feels that Chile can handle. In addition, he is seeking about \$200 million from foreign sources, public or private, for new social programs and balance of payments financing.

5. An important element of Frei's domestic program is agricultural reform intended not only to accomplish the social (and political) purpose of distributing land to landless

peasants, but also to increase production through the more intensive use of the land available, and to develop more effective marketing methods. Related to this is a reform of banking designed to make credit available to small farmers and businessmen. Frei is also committed to a public housing program, to meet an urgent social need, and to the provision of increased opportunities for public education.

6. Despite his popular mandate, Frei's reform program is likely to encounter resistance in Congress, where his party, the PDC, now controls only 28 of 147 seats in the Chamber and 4 of 45 seats in the Senate. Although the PDC is likely to make substantial gains in the congressional election to be held in March 1965, it is problematical whether it can gain control of the Chamber and certain that it cannot gain control of the Senate. Much will therefore depend on Frei's ability to form ad hoc political combinations in support of particular measures.

7. Frei's efforts to achieve long over-due reforms in Chile by constitutional means will be closely watched throughout Latin America. If he should succeed, with US cooperation and support, general acceptance of the Alliance for Progress concept would be greatly strengthened. If he

should fail, his failure would lend support to Fidel Castro's thesis that reform can be accomplished only by violent revolution.*

FOR THE BOARD OF NATIONAL ESTIMATES:



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SHERMAN KENT
Chairman

* Castro has anticipated this result in the following language:

"We will see how this PDC revolution is effected. We will see how they wipe out illiteracy...introduce a program of medical care...reconcile the interests of exploiters and exploited...We will see whether a country's oligarchic and feudal structure can be changed with good wishes, with good intentions...The imperialists apparently want to present the example of Chile as an example countering ours...We are delighted to accept that challenge to see which country progresses more, which experiment goes farther, which solves the real essential problems of the peoples, and how long it takes to solve them.

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Remarks: <p style="text-align: center;">In the light of your conversation with [redacted] -- which I did not hear all of -- I thought you might be interested in the thoughts expressed in this memo. I refer especially to your Sunday night dinner.</p> <p style="text-align: right; font-size: 2em;">(over)</p>					
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was never seen
by OLT.

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Date 9 Oct 64

From Sherman Kent

To: Walt.

The Boss might take
some good from these
thoughts. His dinner is
with a man much
interested in Chile
& its future.

