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The Director of Central Intelligence

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National Intelligence Council

MEMORANDUM FOR: See Distribution

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SUBJECT: Warning Meeting on Latin American Debt

1. Intelligence Community representatives met on 12 October 1988 to discuss economic problems and foreign debt developments in Argentina, Mexico, Chile, and Brazil. Discussion also focused on the prospects for economic structural adjustment to alleviate the debt burden and attract fresh capital to debtor countries.

2. Argentina. Argentina currently is the most troubled debtor. Buenos Aires wants commercial banks to agree to interest capitalization, repayment in local currency, or forgiveness of debt. Banks will try to avoid such unprecedented relief because other debtors, particularly Mexico and Brazil, would demand similar treatment. [redacted] 25X1 25X1

3. Analysts were convinced that reform had progressed as far as could be expected given the political horizon. The political future in Argentina is not conducive to economic reform. Analysts believe Peronist Carlos Menem will win the presidential election. Menem, a populist who advocates protectionism and high wages and has favored a debt moratorium, currently has the backing of labor and the financially pressed middle class, groups that are fed up with President Alfonsin's failed economic policies.

4. Mexico. Representatives expressed concern about President-elect Salinas's ability to ease wage, price, and exchange rate controls without re-igniting high inflation. There was a divergence of views over the political pressure Salinas faces and whether it limits his latitude. [redacted] 25X1 25X1 25X1 There was a consensus that he would drive a hard bargain in debt negotiations.

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5. Analysts agreed that Salinas was committed to economic reform, but differed in their assessments of the impact opposition forces would have on policymaking. [redacted] 25X1 25X1

6. The key short-term concern is the dwindling level of Mexican foreign exchange reserves--especially as oil prices remain depressed and the peso becomes increasingly overvalued. [redacted] 25X1 25X1

7. <u>Chile</u>. Between now and the elections scheduled for 1990, economic policies are unlikely to change but uncertainty over Pinochet's willingness to step down and allow elections will dampen foreign investment and lead to some capital flight. Pinochet's opposition has only vague claims of alternative economic policies. Although the opposition will focus on political rather than economic reform, analysts assume that an opposition victory would lead to more socially-oriented policies and, perhaps, a modification of Chile's current cooperative debt policy. [redacted] 25X1 25X1

8. <u>Brazil</u>. Brazil will register a record trade surplus this year which, coupled with a capital account surplus, will allow it to significantly build reserves. Having secured a commercial bank agreement, policymakers now are focusing on the politically volatile problem of runaway inflation.

9. Brasilia has implemented little structural reform, although there has been much rhetoric regarding trade liberalization and privatization. Although these reforms can permanently reduce inflation over the longer term, progress will be slow given policymakers' short-term focus and the immediacy of the problem. Gaining support for reform will be even more difficult, given the new constitution which gives congress a more extensive economic policymaking role and takes away the President's decree law powers. [redacted] 25X1 25X1

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