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Brazil: Prospects for the Regime

National Intelligence Estimate

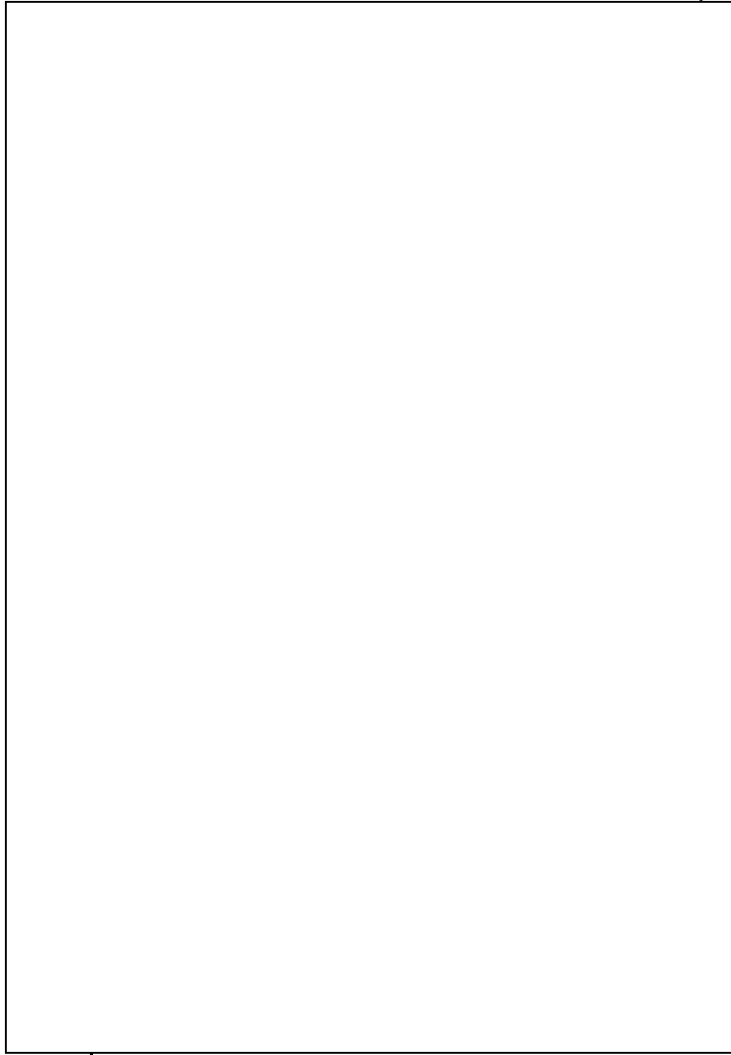
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**BRAZIL: PROSPECTS
FOR THE REGIME**

Information available as of 25 April 1984
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THIS ESTIMATE IS ISSUED BY THE DIRECTOR OF CENTRAL INTELLIGENCE.

THE NATIONAL FOREIGN INTELLIGENCE BOARD CONCURS, EXCEPT AS NOTED IN THE TEXT.

The following intelligence organizations participated in the preparation of the Estimate:

The Central Intelligence Agency, the Defense Intelligence Agency, the National Security Agency, the Federal Bureau of Investigation, and the intelligence organizations of the Departments of State and the Treasury.

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SCOPE NOTE

Brazil—as well as efforts to understand what may happen there—is probably gripped by greater uncertainty today than at any other time since the military took power 20 years ago. Most observers expected that some uncertainty would characterize the period during which the Brazilian military transferred control over the political process back to civilians. No one realized, however, that this would happen at the same time that Brazil was in the throes of its greatest economic crisis since the 1930s.

As a result, the Brazilian Government confronts a variety of forces that have placed it under tremendous stress. This Estimate measures and delineates this stress, assesses what chances the government has for coping successfully with it, estimates what kinds of outcomes may occur over the next year or so, and indicates what these outcomes may mean for Brazil and US-Brazilian relations.

The US stake in whether Brazil makes it successfully through these twin challenges is high. On the economic side, how well Brazil manages its foreign debt—the largest among developing countries, at \$93 billion by yearend 1983—has consequences for the well-being of the international financial system. The direct economic implications for the United States are also large, because US banks hold nearly one-fourth of this debt, and US exports to this extremely important market are in sharp decline. On the political side, it would be a major positive gain for the United States and other democratic nations if the sixth most populous country in the world successfully completed the next-to-last stage in the transition to an open, democratic regime, and a major loss if Brazil returned to repressive military rule or encountered severe political instability.

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KEY JUDGMENTS

The Brazilian Government is faced with two primary challenges over the next year: managing an ailing economy and holding elections for the first civilian president in two decades. In this last year of transition from military to civilian rule, attention will be focused on three central issues:

- The economic prognosis and specifically whether Brazil makes enough progress toward its IMF-mandated retrenchment goals to be eligible for sufficient external funds to get through the next year.
- What rules will govern the presidential election, what are the chances of the most likely candidates, and whether it makes much difference as to which candidate wins.
- The extent to which economic developments are likely to affect politics—specifically, what are the prospects for major political instability, including cancellation of elections, reinstatement of military rule, or massive social protests.

Prospects for the Economy

After 16 years of growth the Brazilian economy has shrunk about 8.5 percent in the last three years. Inflation reached over 200 percent in 1983, and an estimated 25 percent of the labor force had no jobs or were only marginally employed. Brazil's international financial relations are also in difficult straits. By the end of 1983, Brazil had accumulated \$2.6 billion in interest payment arrearages and only narrowly avoided having its US bank loans classified as "nonperforming." (u)

Because of the Figueiredo administration's shortcomings, few Brazilians expect it to accomplish much in its remaining year in office. There is virtually no expectation, for example, that the government will succeed in restoring growth. At the most, hopes seem to be centered

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around the possibility that inflation will drop somewhat and the rate of decline of the economy will slow from the approximately 5-percent drop last year. The international financial community's expectations of the government's performance are not much higher. [redacted]

[redacted]

In our judgment, the fact that these expectations are modest is a good sign that Brazil will be able to maintain political stability at home and obtain adequate financial support from abroad. It means that there is a reasonable chance that most groups within Brazil will continue to cooperate with the austerity program, although very grudgingly, and that foreign financial circles will continue to fund Brazil, even if very reluctantly. For both audiences, decisions about whether to continue to support the Brazilian Government's economic program will revolve more around perceived progress toward meeting 1984 economic goals than on actually attaining mandated or promised goals. For domestic groups, the primary economic indicator of how well Brazil is doing will probably be monthly inflation figures. If they drop to single-digit figures and remain there, we believe there will be a widespread perception that Brazil has turned the corner economically and that the future will be better, even if not in 1984. [redacted]

For the foreign financial community, the main focus is whether Brazil can earn enough foreign exchange to pay at least the interest on its loans in 1984. The key that will be watched here is monthly figures on the trade surplus. If, in 1984, Brazil can significantly increase its exports (the target is by 14 percent over 1983) and can hold imports almost level, then the IMF and foreign bankers are likely to believe that Brazil's economy can eventually grow enough to enable it to manage its foreign borrowing needs successfully. This assumes that no adverse external events occur, such as a rise in interest rates or the price of oil. [redacted]

[redacted]

We believe the chances are reasonably good that Brazil will make significant progress toward meeting its 1984 economic goals, although it will probably not fully achieve any of them. Inflation, for example, is likely to be at least 150 percent—not down to the recently revised government target of 130 percent but a substantial enough improvement to persuade Brazilians to stick with the austerity program.

¹ The holder of this view is the Special Assistant to the Secretary for National Security, Department of the Treasury. (u)

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Similarly, Brazil is likely to run a healthy enough trade surplus during the year to hold the current account deficit to close to the 1983 deficit of about \$6 billion, somewhat higher than the \$5.3 billion target set by the government. Prospects for exports are continuing to improve because of the foreign economic recovery and because the agricultural harvest, especially for soybeans (the main farm export), will probably be much better than in 1983. Still, growing foreign protectionism and sluggish commodity prices will make a 14-percent export growth target not easy to achieve. Whether Brazil can fully reach its target for imports by not permitting them to expand much beyond last year's level is also doubtful. Even with a good harvest there will be increased pressure during an election year to maintain an adequate food supply and, since Brazilian exports have a relatively high import content, more imports than planned may be necessary to prevent industrial material shortages.

Given the uncertainties surrounding these projections, we believe there is a small but not insignificant chance that Brazil's economic performance will be considerably worse than outlined above. In such case, a confrontation would almost certainly occur between Brazil and the IMF, with the IMF possibly demanding additional austerity measures before it would help to reschedule mounting debt or approve new loans. In this circumstance, the Figueiredo administration might attempt simultaneously to placate international bankers by trying to tighten fiscal and monetary austerity and lessen domestic political opposition by replacing the government's economic team. Nationalistic sentiments would be so aroused by a new collision with the IMF and the political atmosphere so heated up by the presidential election campaign, however, that it is doubtful that additional austerity measures, such as new wage restraints, would be accepted by the Brazilian business and political elites.

Even under these circumstances, we doubt that the government would formally break with the IMF and declare a moratorium on debt payment, although such a situation might have come into de facto existence as interest arrearages mounted. The most likely outcome of this situation, in our view, is that the Brazilian Government and the international financial community would use the coming change of administration to postpone resolution of the issues dividing them and that some sort of temporary rescue package, possibly involving the direct intervention of major Western governments, would be put together to prevent Brazil's US loans from being placed in a "nonperforming" category at the end of 1984.

The Presidential Succession

The Brazilian Constitution mandates the indirect election of the president. Despite widespread clamor by the public and by opposition

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political parties for direct elections, we doubt that the Brazilian Congress will muster the two-thirds vote necessary to change these electoral rules substantially. We believe this will not happen because the military appears to be unalterably opposed to opening up the political system that far at this point. It fears in particular that direct elections would permit a leftist politician, such as Leonel Brizola (now Governor of Rio de Janeiro), to become president. We believe that the public and political opposition will be disappointed if direct elections are rejected, but most will continue to concur in the indirect procedure as an acceptable next step in restoring civilian rule.

The chances are good, therefore, that the next president will be chosen indirectly by an electoral college. As a consequence, however, of Figueiredo's weak leadership and the insistence by the progovernment Social Democratic Party (PDS) members that they will make their own decision, Figueiredo has lost the power to impose his successor. With an overall majority in the electoral college, the PDS will retain the inside track for selecting the president if it can unify behind a single candidate during its September 1984 nominating convention.

There is some doubt, however, that the PDS can achieve the necessary degree of unity actually to select a winning candidate. Three candidates have announced for the PDS nomination. The most favored, at this point, appears to be Paulo Maluf, an aggressive PDS federal deputy and successful businessman from Sao Paulo. Maluf is disliked by President Figueiredo, in part because he did not wait for the President's nod before he began campaigning, and Figueiredo so far has refused to support him.

The second candidate is Interior Minister Mario Andreazza, a retired colonel. Andreazza is the preferred choice of Figueiredo, an old comrade-in-arms, and he has support from important PDS political bosses and the head of the National Intelligence Service. Nonetheless, Figueiredo has not come out publicly in his favor, possibly because he doubts Andreazza can win, because his image as a throwback to the worst of old-fashioned politics harms him among government supporters, including those within the military.

Vice President Aureliano Chaves has also recently launched his candidacy for the PDS nomination. He is respected as a competent, if somewhat colorless, administrator and is generally liked in military, government, and business circles for the effective performance he turned in as Acting President on the two occasions when Figueiredo was ill. He is perceived as the most honest of the candidates, which makes him popular among the general public but does not help him with PDS party bosses. He has also gained in popularity as the only candidate who supports a change to direct elections.

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If the opposition political parties do not succeed in their drive for direct elections, they probably will attempt to take advantage of President Figueiredo's unhappiness with the struggle for power going on in the PDS to persuade him to support a "consensus" candidate for the presidency. The major possibility at present for such a consensus candidate is the Governor of Minas Gerais, Tancredo Neves. Neves leads the moderate wing of the major opposition party and is widely respected in all the places that count, including the military. A second possible consensus candidate is Vice President Chaves, if he is denied the PDS nomination and a legal stratagem can be found to permit his nomination by an opposition party. [REDACTED]

With respect to the way in which presidential politics will unfold in the remainder of 1984, however, it probably will make little difference which of the possible candidates are actually nominated by their parties. The positions of all the announced candidates or likely winners are very similar. Virtually all of them, for example, are stressing that Brazil needs to renegotiate its foreign debt on easier terms if economic recovery is ever to happen. None of them is proposing, or is likely to propose, permanently breaking with the IMF, although if economic circumstances worsened considerably, all of them might call for a temporary and conditional moratorium on debt repayment if only as a negotiating tactic. Any candidate with a serious chance to win is likely to be relatively restrained in his criticism of the United States, even if relations with the IMF become difficult, because they would all probably perceive the United States as the only actor that might be able to put together a rescue package that would enable them to avoid having to take office with Brazil ineligible to receive additional international loans. [REDACTED]

The Likelihood of Significant Instability

In our estimation, social unrest is likely to rise during the next year, but not to the level that it will threaten the government's ability to maintain order or to conduct the presidential election. Virtually all groups in Brazil believe they have a significant stake in seeing the election take place and a civilian president take office; and the military is eager to put down the burdens of ruling and return to essentially professional pursuits. In addition, one main aspect of the political culture that has continued even through three years of recession is a relatively low level of political intensity among virtually all groups in the society. In the past, this has led to a high level of tolerance for imperfect regime performance and a tendency not to translate personal aspirations or disappointments into organized political demands. [REDACTED]

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An alternative view, while in agreement with the conclusions of this Estimate, holds that it does not give due emphasis to the risk of serious political turmoil this year in Brazil. According to this view, the growing public campaign for direct presidential elections has heightened the intransigence of both the military and the opposition, and it could delay the negotiation of a political compromise. The holders of this view note, moreover, that a further rise in international interest rates may undermine Brazil's commitment to the IMF-mandated austerity program. Failure to resolve the succession controversy soon, coupled with the necessity of renegotiating the IMF rescue package, could, in their view, lessen the chances for an orderly transition to civilian rule.* [REDACTED]

There are few signs that any of the groups in the society, including politicians, business, labor, the middle class, or the left, are successfully undertaking new kinds of organizational initiatives or developing a new class of leaders that might threaten to overturn these values. The extreme left, for example, which has always been small and weak, seems at a complete loss as to how to take advantage of an ostensibly fertile environment for growth of its influence. What little evidence exists of the attitudes of Cuba and the USSR toward Brazil indicates that neither sees much hope of stimulating significant popular agitation against the Brazilian regime any time soon. [REDACTED]

Some possibility for regime-threatening agitation may occur, however, during the tenure of Figueiredo's successor. If the economy does not recover because another world economic slump or round of tight money policies frustrates even Brazil's best readjustment efforts, or domestic political pressures prevent the new president from bringing about structural changes necessary for restoring growth, then the basic values of the political culture could eventually change. A move to shorten the scheduled six-year term of the new president and choose a new one through direct, popular vote could delay major instability. But if decisionmaking stalemate continued and political chaos ensued, the chances would rise steadily for a return to military rule sooner or later.

[REDACTED]

Relations With the United States

US-Brazilian relations have steadily improved over the last two years or so as Brazil has perceived that the United States is treating it as a mature negotiating partner on a wide range of commercial, nuclear, technological, military, and other matters. Moreover, Brazilian attitudes at the popular and elite levels have remained generally favorable

* The holders of this view are the Deputy Director for Intelligence, Central Intelligence Agency; the Director, National Security Agency; and the Assistant Director, Intelligence Division, Federal Bureau of Investigation. (U)

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toward the United States even as frictions with the IMF and international bankers have developed, because the government and many in the private sector perceive the US Government as essentially an ally thus far in their attempts to negotiate debt relief, obtain new money, and, despite many commercial frictions, expand exports. [redacted]

We believe continuation of good, if sometimes frank, relations will probably persist as long as Brazilians continue to believe that the US Government is doing its best to contain protectionist pressures in the United States, is encouraging the IMF and the banks to be as forthcoming as possible, and is not perceived as attempting to undermine the independent foreign policy Brazil has been following. We believe opportunities to expand relations with the Brazilian armed forces will be especially good if the United States can respond to their professional needs after they reduce their political role. [redacted]

The one area where Brazilian-US relations could most likely become more strained over the course of the next year or so involves Brazil's continued need for IMF support, particularly if its economic performance falls noticeably short of meeting IMF goals. Before and, especially, after the election, there will probably be increased pressure on the United States to support Brazilian requests for a major restructuring of Brazil's debt. These pressures will become very insistent if Brazil fails to recover economically because of events over which it has no control, such as increased oil prices, or a rise in US interest rates or protectionism. [redacted]

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DISCUSSION

Two Decades of Change

1. Some 20 years after having deposed Brazil's last civilian President, Joao Goulart, the Brazilian military is in the process of voluntarily turning over power to a new civilian president and largely removing itself from direct involvement in politics. The modalities of precisely how this will occur and the identity of the next president are still uncertain, but the chances are very good that a presidential election will take place as scheduled in January 1985 and that the new chief executive will take office two months later.

2. The society that the military will return to the control of civilian politicians is far more developed than the one it took charge of in March 1964. In the early 1960s the country was still largely agrarian, and per capita income was low. By 1980, however, per capita income had multiplied more than 250 percent to \$1,650, and 50 percent of the population lived in cities of more than 20,000, as compared with only about 30 percent in 1960. Total energy consumption doubled between 1966 and 1976. The labor force size and structure also changed, increasing by 1.5 million persons annually in the 1970s, as the rate of job creation doubled from the 1960s. By 1980 almost 70 percent of the labor force was engaged in nonagricultural activity, as compared with less than 50 percent in

3. Substantial gains in living standards and welfare were achieved during this period by all economic classes, although severe regional disparities continued and the income gap between rich and poor grew. The educational system was expanded rapidly, as reflected in increased enrollment rates and reduced illiteracy. Social security health programs were strengthened and extended to over 90 percent of the urban and two-thirds of the rural populations; the consequences are evident most notably in declining infant mortality rates. Considerable efforts were also expended on low-cost housing programs for the poor and improved provision of water, electrical, and sewerage services; over 75 percent of urban households—including the occupants of *favelas* (urban squatter slums)—now have piped water and electricity

4. One particularly important aspect of this change was the enormous expansion in the size and influence of government throughout Brazil—especially the federal government. In 1982, for example, the financial resources under the direct allocative control of the federal government were equivalent to 46 percent of the gross domestic product (GDP) of Brazil, a share of the economy seldom exceeded by any public sector in the world outside the centrally planned economies. A large portion of these resources is directed into the production of goods and services not only by government-owned or -controlled firms but also by privately owned firms through transfers to the private sector through such means as subsidized credit. This has given the government the lead role in shaping almost all significant economic activity in Brazil in recent years, including setting investment priorities, influencing sectoral growth, controlling prices and wages, and—as a major employer of labor and purchaser of goods—largely determining labor force composition.

5. During these two decades, Brazil has been a remarkably stable society considering the stresses of rapid modernization through which it has been passing. In part, this stability is attributable to the extraordinary economic growth which took place from 1968 through 1980. Through this period, annual growth dropped below 5 percent only once, and for a number of years it exceeded 10 percent. As a consequence, income disparities between the large number of poor and the rest of society widened, but a more important result was that all sectors of the population benefited from the growth, sometimes spectacularly.

6. The other major underpinning to stability has been the military's success, at least until recently, in creating a governing arrangement that has been largely in harmony with the dominant aspects of Brazil's political culture, in contrast with the populist approach of Goulart a generation ago. Many commentators have noted that the patterns of authority traditionally preferred by Brazilians—from institutions of the family through that of the presidency—have been basically patronal and hierarchical rather than plural-

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ist and democratic. This means that the military's emphasis on governing through large bureaucratic structures, while depoliticizing the middle class, labor, students, peasants, and other mass elements, was essentially congruent with the Brazilian experience of looking to the bureaucracy as a more reliable source of benefits and channel for grievances than to elected officials and political parties. The military's success until very recently in governing in this fashion was also enhanced by another crucial aspect of the political culture: the relatively low level of political intensity in Brazil. This political passivity, which has varied historical and cultural roots, expresses itself in several useful ways for a modernizing military/bureaucratic regime. It leads to a high level of tolerance for imperfect regime performance, a tendency not to translate personal aspirations into organized political demands, and a remarkably easy capacity for co-optation of potential opposition groups by those wielding power.

President Figueiredo's Principal Underlying Problems

7. Both of the conditions that brought stability to Brazil—rapid economic growth and trust in the bureaucracy—have deteriorated sharply since President Figueiredo took office in 1979. While many of the causes of deteriorating stability predate his administration, the shortcomings of his government have exacerbated three weaknesses that are common to bureaucratic authoritarian regimes generally. The first is the **tendency for administrative rigidity to rise as the bureaucracy ages and develops such a degree of autonomy and self-interest that it increasingly fails to respond in a timely way to changing societal needs.** The second is the strong dependence of this kind of system on relatively sensitive and innovative leadership. With so few countervailing powers or other self-correcting mechanisms available in the society—as might be the case if political parties and organized interest groups were stronger—the top leadership must be able accurately to sense changing needs and to meet them. The third weakness is that the long-term legitimacy of such bureaucratic systems rests heavily on their ability to generate a constantly expanding stream of resources to provide the benefits—in the absence of widespread political participation—on which ultimate loyalty to the system frequently depends. The Figueiredo administration is in serious trouble on all three fronts.

Declining Resources

8. For the last three years, Brazil has been in recession. GDP has fallen some 8.5 percent since the beginning of 1981, inflation has more than doubled and is running at an annual rate of over 200 percent, real wages have dropped, and an estimated 25 percent of the labor force have no jobs or are marginally employed. This economic shrinkage has sharply limited the resources available to the Figueiredo administration and has been a major factor in undermining public confidence in its ability to govern.

9. The reputation of the administration has also been badly damaged by its decision to turn to the International Monetary Fund in 1982 for help when it essentially could no longer pay its mounting international bills. For 25 years, Brazilian governments of all political varieties had been consistent in denying that Brazil would ever submit itself to the harsh conditions imposed by the IMF for access to its money. Even after loans from the IMF and commercial banks were obtained, Brazil's international financial relations remained very shaky throughout 1983. A crisis with US banks, arising from the legal requirement to place many of Brazil's US loans in a "nonperforming" category when interest payments on them lagged more than 90 days, was only narrowly avoided late in the year by a revised stabilization agreement with the IMF and negotiation of a new jumbo international bank loan of \$6.5 billion.¹ This secures a large part of the external financing Brazil will need for 1984, but complete disbursement of the money will require further adherence to tough domestic austerity measures, which the Brazilian public will be increasingly loath to accept if economic conditions—such as the rate of inflation—do not soon show some signs of improvement.

Weak Leadership

10. Fundamental doubts about the governing ability of the military—and especially of the technocrats who make and implement Brazilian policy—began to grow a year or so after President Figueiredo took office. The first major blow to the Brazilians' confidence in their leaders occurred when Minister of Planning Delfim Netto was unable to use previously

¹ US banking regulations require loans to be placed in a "nonperforming" category when no interest has been paid for more than 90 days. This adversely affects a bank's earnings and makes it unlikely that it will lend additional money to the debtor. (u)

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successful expansionist economic policies to cope with the drop in growth brought about by the 1979/80 oil price shock. These concerns were compounded by a feud between two top presidential advisers, which led to the resignation of General (Ret.) Golbery do Couto e Silva in August 1981. Golbery was considered by the public to be one of the strongest influences for eventually returning the government to civilian control.

11. The most recent blow to government credibility has been occasioned by President Figueiredo's seeming lack of interest in governing, particularly since early last year. He has failed to exercise leadership on most of the difficult issues the country faces. On the economic side, decisionmaking at the top and down through the bureaucracy has degenerated into day-to-day attempts to cope with immediate problems, and the government's statements about the economy and its program for coping with adversity are largely disbelieved. On the political side, the President has clearly lost control over his own political party and the ability to impose his successor.

A Too-Powerful Bureaucracy

12. Of the three central problems the Figueiredo government faces, the one it is probably least responsible for is the public perception that the civil bureaucracy has developed such power and independence that it is largely out of control. At the popular level, the state enterprises in particular are seen as baronies, led in many cases by retired military officers who have gained vast wealth while heading these companies.

13. The autonomous behavior of the state enterprises does, in fact, complicate Brazil's efforts to overcome its current economic difficulties. While they were well suited to taking on the immense developmental tasks that the government tackled in the days of a rapidly expanding economy, they have been largely unable to adapt to slow or declining growth. Their deficits have been a major source of inflationary pressure, their preferential access to credit has crowded out private enterprise, and their heavy foreign borrowing has contributed substantially to Brazil's indebtedness. Figueiredo has attempted to cut back their role in the economy. But they are so well entrenched that they have generally been able to maintain their operations and personnel rosters, avoid sharp reductions of their official investment budgets, and protect their basic equities.

The Immediate Challenges

14. Very few people in Brazil expect the Figueiredo government to accomplish very much in the year it has left in office. There is little expectation that any lameduck administration could undertake the policy initiatives that would be necessary to attack the economic, political, and social problems of the magnitude Brazil faces. In addition, expectations of the Figueiredo government are greatly reduced because of its perceived poor quality. Consequently, Brazilian elites and masses give the impression that they would be satisfied if the government restricted itself primarily to damage-limiting activities in all three sectors.

15. In the *economic* arena, for example, there is no expectation that the government will succeed in restoring growth in the next year. At most, hopes seem to be centered around the possibility that the rate of inflation—which began to drop in November and December 1983, rose again in January and February 1984, and dropped once more in March—can be further reduced and that enough foreign exchange can be obtained—through a combination of expanded export earnings and, if necessary, new loans—that imports will not shrink further. Both these goals will require considerable activity on the part of the Figueiredo administration and are by no means certain to be achieved, but they are seen as within the reach of even a relatively weak government.

16. *Socially*, the government is expected not to permit a severe deterioration in law and order. Some additional strikes, demonstrations, food-market looting, and even riots are thought likely. Crime in the form of break-ins and robberies, which rose sharply in the last year, is not expected to decline dramatically either as long as there is no improvement in the economic situation. There is the expectation, however, that the federal government will help provide enough resources to the state governments and municipalities to prevent any sudden, further deterioration in security for the individual. There is virtually no belief that the Figueiredo government will take measures to reduce corruption, aid education or health services, or otherwise improve social conditions for the middle class or the poor.

17. There is one general expectation in the *political* arena that seems to be held by all sectors of the Brazilian public: that the government will continue to do all it can to further the process of political liberalization (*abertura*) so that a civilian president can take

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office in March 1985. In many respects, toleration of the Figueiredo administration, with all its perceived ineptitude, rests on the belief that the President is committed to this goal.

18. There is considerable public interest in what form the January presidential elections will take and in the maneuvering that is taking place among the political elites as they jockey to strengthen the position of one candidate or another. However, while the general public may prefer direct elections, it will acquiesce in indirect elections as a reasonable next stage in the political liberalization process. Significant public alarm would probably occur only if Figueiredo were seen to be backing away from his commitment to liberalization, or if it appeared that he were losing control over elements of his administration that might favor continuation of military rule.

19. In the immediate aftermath of successfully completing negotiations with the IMF and commercial banks for the \$6.5 billion in new foreign loans that will be disbursed to Brazil in the next few months, *foreign policy* questions do not rank high on the government's immediate action agenda, or in the perceptions of the public. In fact, with the exception of foreign economic policy, foreign policy issues are seldom the focus of attention in Brazil, because foreign policy has been based on a relatively broad and unchanging consensus, because it has been perceived as clearly furthering Brazil's basic interests, and because it has been carried out in a generally skillful and nonconfrontational manner. Moreover, neither Brazil's economic difficulties nor the uncertainties involved in making the transition to a civilian government are having any immediate impact on its noneconomic foreign policy goals. These include its efforts to maintain good relations with Argentina and the countries of the southern cone of Latin America generally; to guard against the development of any security threat on its borders (as it is doing in Suriname); to maintain good relations with the Arab states (especially Iraq) that are its main sources of oil; to avoid strong leadership positions on North-South issues so as not to create counterproductive bilateral tensions with any possible source of markets, technology, or money; and, while remaining clearly anti-Communist, to maintain as wide an array as possible of good relations with countries of varying ideological positions.

20. Foreign economic policy, except for management of the foreign debt, is also essentially uncontro-

versial. There are concerns among businessmen that Brasilia not agree to cut back too quickly on export subsidies and other government types of assistance that help make Brazilian goods cost competitive in the international market. And there also was unhappiness with the way in which the central government took control in 1983 of all foreign exchange transactions (the decree was recently revoked), which made it extremely difficult for many Brazilian businesses whose goods have an import component to pay their bills and obtain the needed foreign ingredients in a timely fashion. These specific problems have been compounded for both Brazilian and foreign businessmen by the seemingly erratic and inconsistent way the Brazilian bureaucracy has interpreted and implemented constantly changing rules and regulations as the government has attempted to cope with the growing economic crisis. Nonetheless, there is little fundamental opposition to the notion that the country's economic well-being depends significantly on Brazil's ability to export, and that the primary function of foreign economic policy is to obtain the necessary markets and to facilitate sales.

21. Brasilia's approach to handling the country's massive foreign debt is another matter, however. Criticism has grown in the last year or so concerning what is perceived as the unchecked arrogance and the grandiosity of the technocrats who contracted the debt over the years and, particularly, their stubborn refusal to recognize when world economic conditions had changed in a way which should have led to a more modest Brazilian approach to financing growth through foreign borrowing. There is also much grumbling about the way in which the Brazilian Government economic team has negotiated with the IMF. Brazilian private-sector businessmen, in particular, believe that Delfim Netto and his associates have not represented Brazil's interests well. While there is broad agreement on the need for austerity and even with some IMF objectives (such as cutting public-sector spending), the team is criticized harshly for accepting unrealistic targets (such as an earlier agreement to attempt to lower the inflation rate to 50 percent in 1984) and for failing to make any significant effort to restructure the entire foreign debt. The apparent success of the government in securing the new loan package from the IMF and commercial banks has momentarily muted some of this criticism. But distrust of the government is so pervasive it is certain to rise to new heights if Brazil has to return to

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the international banking community to secure additional loans to make it through 1984. If that becomes necessary, renewed criticism of the government's economic team and its strategy is almost certain to arise from the business community, the politicians, labor, the middle class, and even some in the military and among the technocrat [redacted]

The Current Political Dynamic

22. Some of these groups were once part of the coalition that has governed Brazil since the military takeover in 1964. That coalition has changed in recent years and months, however, as some partners have dropped out and the balance of power among those who remain has become much more complex. At present, the number of groups involved directly and actively in national-level politics is relatively limited. Those most active now are a small ruling elite surrounding the President and a small but expanding number of ostensibly progovernment and opposition civilian politicians. Most other groups, including the bulk of the military, businessmen, and the middle class, have become essentially political bystanders, even when they are vocally opposed to the government [redacted]

The Ruling Elite

23. For most of the period since 1964, relations among the groups that make up the ruling elite have been fairly orderly, with power clearly centered in the hands of the President and his closest advisers. In recent years, however, these relationships have changed quite sharply. **Decisionmaking power**, for example, is much more fragmented. Technocrats manning the ministries and the state enterprises now represent, after 20 years of growth and accumulation of resources, a separate power base, no longer directly dependent on the military for their positions and authority. The politicians, as an outcome of the gradual transition back toward civilian rule, have also acquired separate interests and an independent political base now that they have popular constituencies to represent and to answer to. At this stage in the political transition process there is no center of gravity: the military is withdrawing from direct involvement in politics, the bureaucracy is strong enough to protect itself from outside control but does not have the power of initiative, and the politicians are powerful enough to interfere with the wishes of the executive branch but are not yet strong or well organized enough to impose their authority [redacted]

24. Normally, Brazilian presidents could exercise sufficient leadership to cope with even this amount of confusion if the President exercised the power available to him. [redacted]

[redacted] As a consequence of this disarray within the ruling group, there is widespread uncertainty about what kinds of policies the administration will pursue, the vigor with which it will enforce the laws and regulations it ostensibly supports, and how it will cope with opposition to its programs. [redacted]

25. This kind of political situation offers clear incentives for bargaining, particularly between the executive and legislative branches. One of the strongest signs that the Brazilian political system will be able to survive the current crises is that, as happened with congressional passage of a restrictive wage law demanded by the IMF and in an increasing number of other areas, real negotiations between the executive and the legislature have begun to occur. A collective sigh of relief could be heard from the Brazilian public and from most foreign observers when agreement on the wage bill was finally reached, for example. There had been widespread fear that either complete decisionmaking paralysis would grip the policymaking machinery if neither side would give in, or that the government would be tempted to impose its will by unconstitutional means, setting back *abertura* and threatening a return to repressive government. Since the Brazilian Congress and the major political parties are led by political moderates and since the President remains fundamentally committed to the restoration of civilian political rule, the prospects that they will be able to continue to resolve differences for the rest of Figueiredo's term—unless the President seeks tougher

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new austerity measures—are relatively good. Nonetheless, considerable friction will almost certainly occur during this process, and uncertainty over final outcomes will remain high because both sides are inexperienced at this kind of bargaining and, in these changing political circumstances, are not sure of their respective strengths. [redacted]

The Political Class

26. The prospects and influence of professional politicians have revived strongly enough in the last year or so to allow them to be thought of, after 20 years in the wilderness, as significant political actors. Partly because they have been powerless for so long and partly because they are riding a wave of tremendous popular sentiment in favor of restoring civilian rule, they are successfully demanding a larger role in the political process. Some of their energies are consumed by strong rhetoric focused on attacking the government's economic team and the alleged disastrous effect its policies are having on the well-being of the middle class and poor. The opposition parties have, for example, passed a nonbinding resolution decrying the IMF austerity program and advocating a break in relations with the IMF. These activities, while they contribute to the perception that the government is beleaguered, do not seriously affect relations between the administration and Congress. [redacted]

27. In other matters, however, the politicians have become a force with which the executive branch must reckon, especially since Figueiredo cannot take the support of the "progovernment" Social Democratic Party (PDS) for granted. Although the five political parties represented in the federal Chamber of Deputies ostensibly divide between 235 members of the PDS and 244 members of four opposition parties, this distinction blurs in practice. The administration frequently finds that it must negotiate at least as vigorously with the leaders of its own party to achieve passage of needed legislation as it does with leaders of the opposition, because congressional members of all political stripes have developed institutional loyalties to the Congress that take priority over party differences when, in struggles with the executive branch, they feel their prerogatives as legislators are being ignored. [redacted]

28. Executive-congressional relations are further complicated by the President's strong dislike for the apparent preference of a majority of the PDS for the presidential candidacy of Paulo Maluf, a PDS federal deputy from Sao Paulo. Figueiredo's bitterness over PDS support for Maluf has caused him to state that he

is no longer willing to oversee the choosing of a PDS presidential candidate and that it might be appropriate to engage in consultations with a wide range of civilian groups, including members of the political opposition, before a presidential nominee is selected. This at least suggests to the PDS that he would be willing to make a deal with the opposition political parties to name someone not supported by the PDS as a "consensus" presidential candidate, thereby taking the power of presidential choice away from the PDS. [redacted]

The Military

29. For most of the last two decades, military officers, because of the perceived close link between national security and national development, have generally believed their institutional interests were virtually identical with those of the government and that their primary role was to maintain firm hierarchical discipline in support of the President and his advisers. In the last two years, however, senior officers have become increasingly disturbed by the government's lack of direction and, particularly, Figueiredo's failure to provide leadership during this period of increasing economic trouble and political uncertainty. They fear that the military will be more and more blamed for the country's problems, thereby further damaging its reputation in the eyes of the public. Stimulated by events in Argentina, they are also concerned with rising popular reaction against corruption in government, some of which is directed at those military officials who hold office in the ministries and state enterprises. This concern about corruption extends down through the ranks, with some middle- and junior-grade officers beginning to worry about the effects on their careers of loss of public esteem for the military. [redacted]

30. The stress of being targets of public criticism is creating some dissension within the military. Nonetheless, despite signs of internal division, the Brazilian military high command remains loyal to Figueiredo, and hierarchical discipline within the ranks is strong. Unlike in earlier years, there are virtually no "hard-line" officers left in the higher ranks around whom disgruntled officers can rally. Virtually all officers continue to support further political liberalization and a return to civilian rule, because they see that avenue as the only way the military can regain its professional orientation and its historically good reputation. [redacted]

31. Some top officers are concerned that, after the military leaves power, the civilians might be tempted to examine "human rights" violations during the two

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decades of military rule, as is happening in Argentina. There is also widespread determination that the left, in the person, for example, of former "subversive" Leonel Brizola, now Governor of Rio de Janeiro, not be permitted to run for president.

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sion of aborting the *abertura* process, however, because military officers generally believe that they will retain enough influence even after they have returned to the barracks to prevent these things from occurring.

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its own members as possible substitutes for the current economic team; nor has it tried to unite behind a presidential candidate sympathetic to private-sector interests.

34. Most other sectors of the Brazilian public are even less politically active than the business community, and there are few signs that any of the sectors are undertaking the kind of organizational initiatives or producing the leaders that might bring about such activity. *Organized labor*, the *middle class*, and even what little exists of an *extreme left* (see inset on next page) all seem to be concentrating on finding ways to lose as little as they can in the present difficult times rather than seeking ways for an immediate reversal of present economic and political circumstances. Even the *Catholic Church*, which three years ago or so was developing grassroots community organizations that might have some political potential, now seems to be concentrating on encouraging self-help projects among the poor and longer term educational programs with labor that have little immediate relevance to national-level politics.

The Bystanders

32. Brazilian *businessmen* are massively unhappy with the Figueiredo administration. Antiadministration feelings, already high because of business perceptions of inept government performance, have been exacerbated by businessmen's beliefs that Planning Minister Delfim has failed to demand or at least to negotiate strenuously for more lenient conditions on IMF and commercial bank loans and, in particular, that Delfim has treated the business community in a cavalier way. They believe, for example, that the costs of austerity have been placed much more heavily on the private sector than on the many businesses run by the government and that even modest growth rates cannot be restored until spending by state enterprises is brought under control. They also believe Brazil's foreign debt must be restructured if growth is to return.

35. There is one general sentiment that all sectors appear to share. That is a strong desire to return to a fully open, competitive political system headed by a directly elected civilian president. While deeply disturbed by the economic sacrifices that are being visited upon the middle class and the poor, and alarmed by the drift in government and the national-level leadership vacuum they perceive, most people believe that Figueiredo and his government remain committed to continuing the *abertura* process. Many express doubt that the country can generate the kind of sustained effort that will be necessary to turn around the economic situation until there is a directly elected president who will have the political clout to rein in special interests—particularly what they claim is a bloated and unresponsive public bureaucracy. Nonetheless, indirect elections for president are an acceptable way station as long as momentum toward eventual direct elections does not come to a halt.

33. Despite the intensity of their opposition to the government, however, businessmen have engaged in relatively little political activity beyond rhetoric. The influential Sao Paulo State Federation of Industries, for example, has not developed its own comprehensive program for combating the recession or boosted any of

The Coming Year

36. As Brazil enters the last year before its scheduled presidential election, there is a rising level of uncertainty about how the economic situation and its political consequences, on the one hand, and the presidential succession issue, on the other, will resolve

The Extreme Left in Brazil

The extreme left in Brazil is remarkably small and weak considering the fertile ground for its activities that might be thought to exist because of widespread and growing economic discontent. Both the middle class and the poor, despite their frustrations, remain extremely difficult to organize for any purposes, and they show no signs of being attracted by leftist causes or values.

Even if the poor and the disappointed middle class were more susceptible to leftist appeals, the radical left in Brazil is not in a position to take advantage of growing economic and social discontent. It suffers from three main problems:

- The government's program of political liberalization has taken away the antiauthoritarian issue on which it might have been most vulnerable.
- State dominance over the Brazilian economy is so extensive that there is little room on the left to agitate for greater socialist control.
- Radical leftist groups are so racked with internal dissent and penetrated by government security and intelligence organizations that it would be very difficult for any of them to pose a serious threat.

The largest of the extreme leftist groups, the Moscow-line Brazilian Communist Party (PCB), probably has fewer than 10,000 members and considerably fewer activists. It is striving so hard for legalization (a very unlikely prospect) that it has become a force for moderation, cautioning the left against general strikes, student protests, or civil disturbances.

Other groups on the extreme left are even weaker, generally having only a few hundred members. Some have attempted to exploit street riots and foodstore lootings, but none has the capability to organize them. A few of them have displayed banners at large public gatherings organized to support direct elections, but the organizers have generally been careful to force them to the fringes of the crowds in order not to provoke a government reaction.

Active foreign involvement with the extreme left in Brazil appears to be minimal. What little evidence exists of the attitudes of Cuba and the USSR toward Brazil indicates, for example, that neither government believes there is much hope of stimulating significant popular agitation against the Brazilian regime any time soon.

themselves. On the economic/political side the major short-term questions are:

- How likely is it that Brazil will make consistent enough progress toward its IMF-mandated re-trenchment goals to persuade the banks to disburse the entire \$6.5 billion new loan package completely and on time?
- In the absence of sufficient progress or in the case that new loans are needed from the international community to enable Brazil to get through 1984, what additional austerity measures might be required? To what degree are pressures for a unilateral moratorium on payment of the debt likely to grow?
- What economic signs would persuade Brazilian businessmen and the public that enough progress was being made toward stabilization to make the government's austerity program worth continuing to tolerate and accept sacrifices for? Are there conditions under which business, other elites, and the public would accept additional sacrifices?
- Does the government have sufficient political clout or maneuvering room to maintain compliance with its stabilization program or to gain acceptance of new austerity measures?
- What happens if it does not?

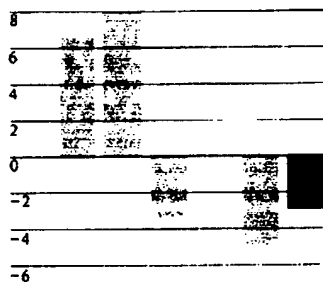
Economic Challenges and Uncertainties

37. *Entering the Critical Phase.* Brazilians may have passed through something of a watershed in November and December of last year when glimmers appeared that the worst of their economic downturn might be behind them. The rates of inflation for November and December (8.4 and 7.6 percent, respectively) dropped from previous months, a target of \$6 billion in trade surplus for the year was slightly exceeded, agreement on the new jumbo loan was reached, and a growing number of businessmen (especially in Sao Paulo) acknowledged that the recession had caused them to become efficient enough to begin to make a profit (or at least to stop losing money). Clearly, these are very fragile signs of a turnaround. They could prove to be momentary blips in a continued deepening recession if no real progress is made on the fundamental causes of the economic contraction, such as the size of the public deficit, or if adverse external events occur, such as a rise in oil prices or international interest rates. Nonetheless, these signs

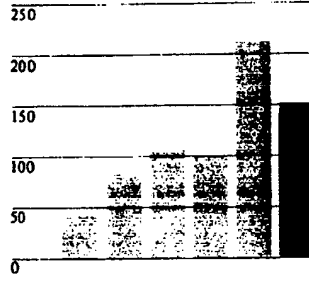
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Brazil: Economic Indicators, 1975-84

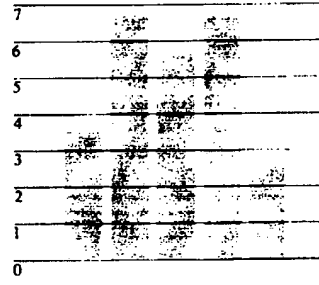
Average annual percent
Real GDP Growth



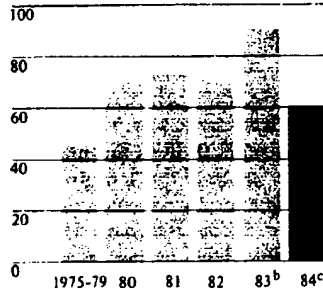
Note change in scales
Consumer Price Growth
December to December



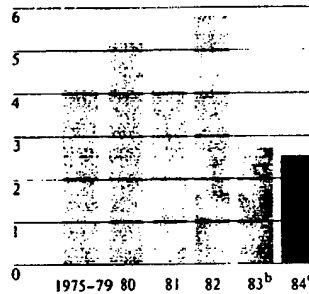
Government Deficit As a Share of GDP^a



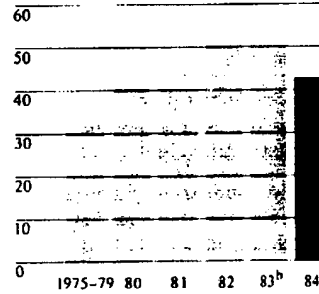
Money Supply Growth
December to December



Current Account Deficit As a Share of GDP



Oil Imports As a Share of Total Imports



^a Excludes inflation adjustments to value of outstanding public debt.

^b Estimated

^c Projected

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have had a positive psychological impact in a country where buoyant optimism about the future has been an important underpinning of past economic growth and political stability. (See charts of economic indicators.)

38. These breaks in the gloom, combined with the holiday spirit and congressional recess that accompany the Christmas-through-Carnival period, led to a three-month respite in public and congressional concentration on how bad things are economically and, consequently, to a lessening of immediate pressure on the government. During this period the government announced a number of budgetary steps for 1984 that aim at lowering government expenditures in the year

ahead. These measures, which include ending interest rate subsidies for agriculture and all exports and further cutting state enterprise investment, are designed in part to reassure foreign investors and debt holders that Brazil will pursue austerity in 1984 with at least as much vigor as it did in the last half of 1983. They are also a signal to the Brazilian public that the government intends to continue to move forcefully to make structural adjustments in the economy despite the sacrifices these adjustments call for.

39. The real test of the government's commitment to continued austerity and, particularly, its ability to manage the stabilization program successfully will probably begin sometime early in the second quarter

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of 1984. By that point, presidential succession politics will have heated up, and it will become more apparent how much of an issue presidential candidates will make of the government's handling of the economy and how much new resistance there will be in Congress and among important elites to holding firm on austerity.

40. By the beginning of the second quarter of 1984, enough evidence will also have accumulated to begin to draw conclusions about how closely Brazil is conforming to the economic targets to which it has committed itself for 1984. Some of these targets were established as part of the last IMF agreement and will be used as benchmarks for periodic release throughout 1984 of a little less than half of the \$6.5 billion jumbo loan. The three major IMF-imposed targets are:

- Reducing the expansion of the money supply and the monetary base from nearly 100 percent in 1983 to only 50 percent in 1984.
- Cutting the public-sector borrowing requirement from 18.6 percent of GDP in 1983 to 11 percent in 1984.
- Devaluing the cruzeiro throughout 1984 at a rate at least as great as percentage increases in Brazilian inflation.

41. A number of other targets are self-imposed rather than formally part of the Brazil-IMF accord. Nonetheless, they are at least as important as the IMF-imposed goals since they are more visible and will probably be used by the Brazilian public and by foreign observers as the handiest marks for judging the degree of success of the austerity program. In particular, the government's targets of holding the rate of inflation to 130 percent in 1984 and restraining the current account deficit to \$5.3 billion² will be watched closely. (u)

42. All of the goals—both those that are part of the IMF agreement and those that are less formal—are extremely ambitious, and Brazil would be in deep trouble if there were serious expectations that the country would be cut off from foreign loans unless they were precisely reached. We believe, however, that judgments both within Brazil—as to whether to continue to cooperate, even though grudgingly, with the austerity program—and in foreign financial circles—as to whether to renegotiate overdue debt or to

² The Brazilians do not count reinvested earnings in calculating their current account balance. (u)

loan new money, no matter how reluctantly—will turn more on perceived progress toward meeting the targets than on actually attaining them.

43. Many of the factors that will determine how close Brazil will come to meeting its adjustment goals will be seriously affected by external developments not under Brazil's control. This is particularly true of the effort to reduce the current account deficit to \$5.3 billion, which turns largely on Brazil's ability to attain a trade surplus of over \$9 billion in 1984 by raising exports at least 14 percent from last year while holding the import bill to about the same level as in 1983. Generating this kind of trade balance depends in part on how aggressively Brazil markets its products, such as military goods, and how successful it is in arranging additional countertrade exchanges, such as the arms-for-oil deals it has with Iraq and Libya. But it depends probably even more on how open foreign markets remain to growth in Brazilian industrial products, such as semifinished steel, and commercial goods, such as shoes and textiles. Another factor over which the Brazilians have little influence will be the prices they will receive for such key agricultural exports as soybeans, orange juice, coffee, and sugar. On the import side, it is essential that Brazil try to trim \$1-1.5 billion from its oil import bill in order to divert that money to buy other imports for replenishing low stocks of critical raw materials and intermediate goods, many of which are used for the production of exports. This will depend in part on Brazil's ability to increase rapidly rising domestic oil production from last year's average of 337,000 barrels per day to a yearend target of 500,000 b/d. But it is equally crucial that world crude oil prices, over which Brazil has no control, remain steady, because every \$1 increase in the price of oil adds \$250 million annually to Brazil's import bill.

44. At the moment, prospects for achieving the export target of \$25 billion look uncertain, although exports will almost certainly grow from last year. A sharp reduction in petroleum imports and a strong surge in exports of finished and semifinished goods did combine to yield record trade surpluses in January, February, and March, but protectionist forces in the United States and Western Europe seem to be growing. In addition, after a sharp decline in agricultural production in 1983 because of droughts and floods, harvest prospects for 1984 are greatly improved. The possibility that the soybean crop will be close to record proportions is especially important because the Brazilians are counting on that one commodity alone (in

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which they compete with the United States to be the world's leading exporter) to produce some \$3.5 billion in foreign exchange earnings.³ Reaching this goal depends at least as much on price as on quantity, however, and here the indicators are not as good. As of late January, beans that had sold for \$360 a ton last September were getting only \$280 a ton. This could drop earnings from soybeans to \$2.7-2.8 billion. Soybeans will enter the world market in April, pointing again to the second quarter of 1984 as a critical time for the Brazilian economy. [redacted]

45. With respect to that part of the economic picture that is much more under Brazilian Government control—especially effective management of programs to achieve reduction of the public-sector deficit, cut the money supply, effectively devalue the cruzeiro to maintain export competitiveness, and restrain overall the domestic forces that feed inflation—we expect the government to turn in a mixed performance. Very few people either in Brazil or abroad doubt the Figueiredo administration's commitment to pursuing austerity—and that is an important accomplishment that will work in the government's favor with foreign lenders. Nonetheless, there is considerable doubt about its ability to carry out effectively the many useful steps—such as reducing state enterprise spending and suppressing wage increases—that it has initiated to stabilize the economy. Moreover, normal slippage due to government inefficiency and susceptibility to pleading by special interest groups will probably increase because of the efforts of various parts of the government to provide an advantage to the political candidates they favor as presidential politics intensify. In addition, if some of the austerity measures really succeed—especially reducing the budgets of state enterprises and ministries—they, at least at first, will have a further recessionary impact on the private sector because its biggest customer for goods and services is the public sector. To avoid alienating the private sector entirely, the government may be tempted to compensate by loosening somewhat the squeeze on credit, prices, availability of foreign exchange, and imports. [redacted]

46. As a consequence of this slippage, we doubt Brazil can cut inflation to less than 150 percent. Higher-than-projected inflation, in turn, will further hinder prospects for achieving the public-sector bor-

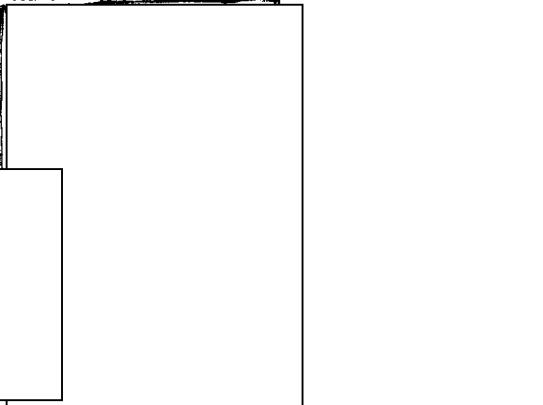
³ Soybeans and soybean products are Brazil's most important agricultural export. Coffee, the agriculture export commonly associated with the country, ranked second in 1983. (u)

rowing drop required by the IMF agreement. In addition, we doubt that Brazil can hold the current account deficit to \$5.3 billion, although we believe it will probably not significantly exceed last year's deficit of \$6.2 billion. Our major doubts here involve whether Brazil can achieve fully:

- The level of agricultural exports planned in view of the need to maintain adequate domestic supplies during a year of political ferment.
- The minimal expansion forecast for imports in view of possible bottlenecks for production of exports that could result from industrial material shortages.

Overall, we believe the most likely economic growth scenario for Brazil in 1984 is a decline of 2 to 3 percent, better than the drop of approximately 5 percent in 1983 but still not a return to positive growth rates. [redacted]

47. *Relations With the IMF.* In our judgment, economic performance in this range will probably be perceived as reasonable by the foreign financial community, and Brazil will be able to proceed with its stabilization program with its foreign creditor backing generally intact despite missing some performance targets. We believe that the IMF will accept—and the Brazilians are certain to insist on this—that the government has done the best it can under the circumstances, even if that means Brazil will need additional loans to get through 1984. [redacted]



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48. Given the uncertainties surrounding these projections, we believe there is a small but not insignificant chance that Brazil's economic performance will be considerably worse than outlined above. Most likely this would occur if there were a convergence of

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adverse world economic trends, domestic political pressures, and gross economic mismanagement by Brasilia. In such a case, a confrontation would almost certainly occur between Brazil and the IMF over attempts to require additional austerity measures that the IMF would believe are essential before negotiations could even seriously begin on rescheduling debt and obtaining the additional foreign loans Brazil would need. In this circumstance, the Figueiredo administration, which has staked its entire political reputation on maintaining good relations with the IMF and foreign bankers, after negotiating strenuously might attempt to introduce decrees and legislation embodying new austerity measures such as further wage restraints. Simultaneously, it might make such gestures to placate domestic opposition as replacing the current economic team and, possibly, offering to support an opposition candidate for the presidency in exchange for congressional passage of the new measures. []

49. By this time, however, nationalistic sentiments in Brazil would be so aroused, support for austerity so low among virtually all elites, and succession policies so far along that it is dubious the Figueiredo government could get the backing it would need to reach agreement with the IMF. We doubt that, even under these circumstances, the government would formally break with the IMF and declare a unilateral moratorium on debt payment. Such a situation would have probably come into de facto existence, however, because negotiations with the IMF and the banks would be stalemated, and Brazil would probably be falling further and further behind in meeting its repayment schedule. []

50. In this turmoil, the chances might increase that either elections would be canceled and authoritarian rule reimposed—so that the government could obtain the power it would need to increase austerity—or a sudden move in exactly the opposite direction would occur toward direct elections. We doubt, however, that either of these options is very likely. If anything, we believe these conditions would intensify the already fervent desire of the military to get out of politics and shed the responsibility for coping with complex governing problems. We believe the military would, nonetheless, take forceful measures, if necessary, to contain social riots and protests, including intervening governments in major urban areas such as Rio de Janeiro and Sao Paulo if protest activities there began to escalate significantly. This would probably be

done, however, as an effort to keep the political process moving ahead, rather than to end it. On the other hand, direct elections in this kind of superheated atmosphere would probably not be acceptable to the military and other conservative groups, who would fear that antimilitary leftist or populist figures, such as Brizola, might gain election in such conditions. []

51. The more likely outcome, in our view, would be that elections would occur on schedule, and that the Brazilian Government and the international financial community would use the coming change of administration to postpone resolution of the issues dividing them. Some kind of eleventh-hour financial package, possibly involving the direct intervention of major Western governments, would be put together so that Brazil's US loans would not be classified as "nonperforming" at the end of the year. But the stalemate between Brazil and international lenders would have led to severe new recessionary pressures in the Brazilian economy. []

52. *Signs To Watch.* Brazil's economic performance in the early months of this year will be critical to the government's willingness and ability to stay its present austerity course. Following are some of the important signs to watch in order to see in which direction the economy is going:

- The rate of inflation. Inflation for January was a little under 10 percent, somewhat more than the government had expected. In February it rose to 12.3 percent and in March it dropped again to 10 percent. A clear drop to single-digit price increases in the next two or three months would support the notion that recovery is under way. A steady drop in inflation is probably the single most important thing that could persuade Brazilians that economic retrenchment is working and should be supported. The failure of inflation to decline will similarly be read as the failure of austerity, and even grudging acceptance of such policies as wage restraint will sharply diminish.
- The size of the soybean harvest and Brazilian ability to sell the crop at good prices before the US crop comes on the market.
- The strength and openness of the United States and, to a lesser degree, the remainder of the OECD market for Brazilian industrial products.
- The composition of Brazilian imports to see if oil imports can be cut back and material essential

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for exports increased without greatly increasing the import bill.

- The degree of government success in cutting back the operating deficits of the state enterprises. Investment outlays, because they are big and highly visible, have been easier to target, but the real test of Figueiredo's efforts to gain control over the public sector will be the extent to which his administration can reduce day-to-day operating expenditures for such things as wages and employee benefits.
- International interest rates, because every 1-percent rise in the rate Brazil pays on its foreign debt costs the country \$750 million.

The Presidential Succession

53. *Chances of Drastic Procedural Change.* At one point in the past year, the question of how Brazil would choose its next president appeared so unsettled that even drastic proposals, such as switching to a parliamentary system in which leadership power would be divided between a prime minister and a president, were at least mentioned in some top political circles. As the time horizon shortens, however, selection processes that would require radical changes in election or other laws become less and less likely. By this point, it appears possible virtually to rule out a switch to any procedure that would require a constitutional amendment to bring about. This eliminates a change to a parliamentary system, a realignment of the political party structure to create a new party of the center that would offer a widely backed, "moderate" candidate, and, increasingly, a move to direct presidential elections in January 1985. The idea of direct elections did receive a major boost in November 1983 when Figueiredo announced that he, in theory, preferred that procedure to the present indirect process. Opposition politicians, including all the non-PDS governors, spoke out strongly at that point for a change to direct elections, and there has been a groundswell of public support for the idea. In particular, major public demonstrations in favor of direct elections have been held in several cities since January. This campaign is designed to peak in late April, when Congress is to vote on a proposed constitutional amendment to permit direct elections.

54. The chances that the change to direct elections will actually occur, however, are slim. The military has let it be known it does not favor taking the risk of opening the political system that far at this time. PDS politicians show no signs of being willing to let go of

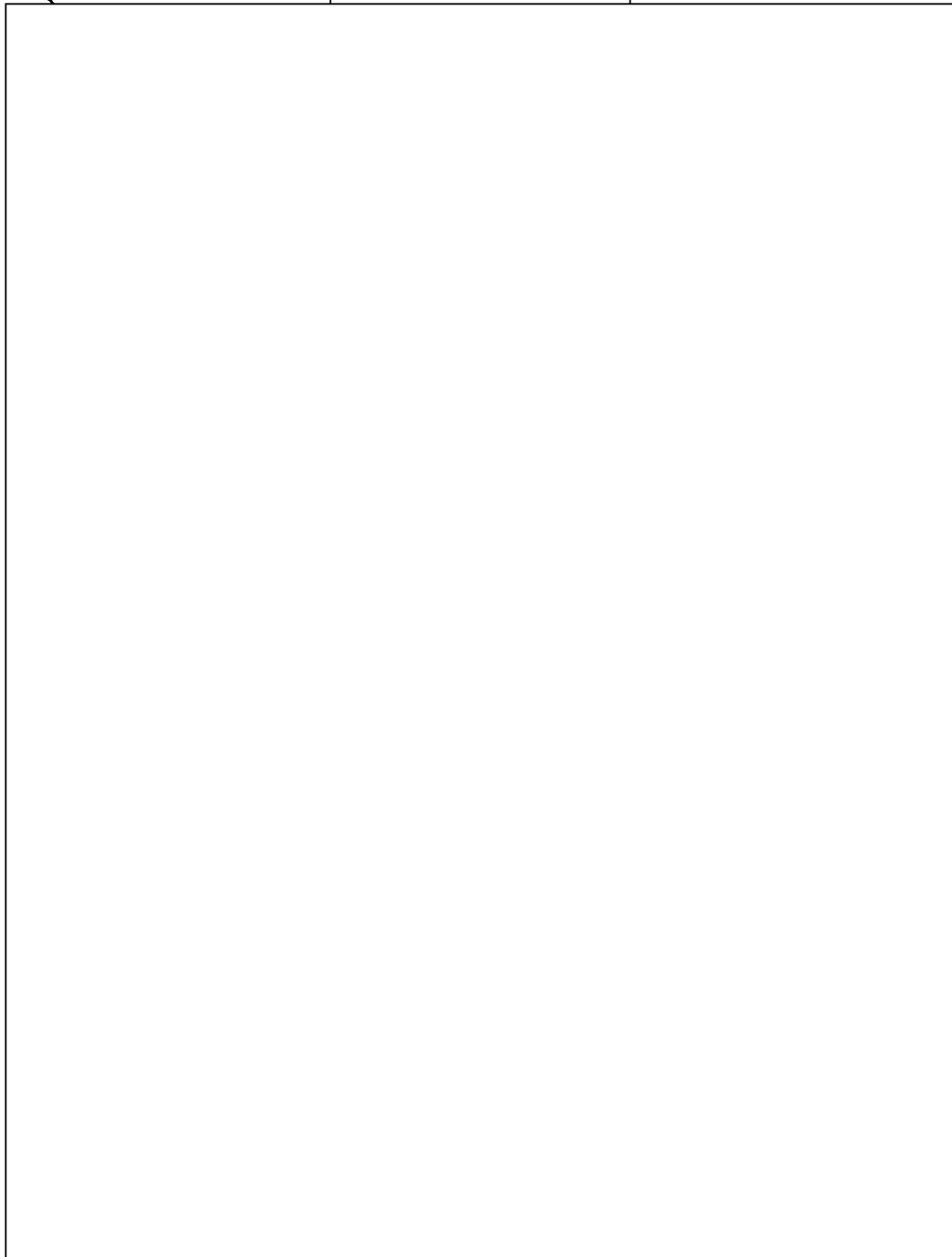
their presumed advantage in choosing the next president through their voting majority in the electoral college. And no powerful individual (such as the President, who was persuaded by the military high command to withdraw support for his own idea) or any significant political group in the legislature has stepped forward to work forcefully for the two-thirds vote in the Chamber of Deputies and the Senate that would be required to institute the direct electoral process.

55. *Most Likely Indirect Scenarios.* The two most likely scenarios for choosing the next president feature, therefore, different kinds of contests for the votes of the 686 individuals who make up the electoral college. The first major scenario, which rests on a straight-line projection of the current status quo, would involve a struggle among several candidates to win the PDS nomination at their September 1984 party convention, with election to the presidency following almost automatically in January 1985 because of the PDS control of the electoral college. Right now, the three major candidates for that nomination are Paulo Maluf, the aggressive PDS Deputy from Sao Paulo; Interior Minister Mario Andreazza; and Vice President Aureliano Chaves. (See next page.)

56. By most accounts, Maluf has a solid lead in rounding up the necessary votes for nomination, and he has claimed commitments from a majority of delegates. His strength derives from his early start in hard campaigning, his astute mixing of modern political techniques (such as computer-based delegate lists) and old-fashioned favor granting, his large personal fortune, and his "take charge" leadership image.

57. Andreazza's candidacy, which has been very slow to take off, received a major boost in February when a political boss in the Northeast, who controls 60 PDS convention votes, unexpectedly declared in favor of Andreazza rather than Chaves. Andreazza is the preferred candidate of those among the technocrats and within the PDS who would like to see the least possible change in who governs Brazil and who has access to the public coffers as the country shifts from a military/bureaucratic to an ostensibly more open, civilian-dominated political system. He was initially hurt by Figueiredo's failure to designate him as the government candidate, but his candidacy remained alive because Figueiredo did not come out in favor of anyone else either. Despite Andreazza's recent gains, Maluf probably remains the favorite in the PDS, because Andreazza's image as a throwback to the

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worst of old-fashioned politics harms him among government supporters, including those within the military.

58. Vice President Chaves announced his candidacy in early February but has only begun to campaign, and his strength is difficult to measure. He is respected as a competent administrator and is generally liked in military, government, and business circles for the effective performance he turned in as Acting President on the two occasions when Figueiredo was ill. He is perceived as the most honest of the candidates, which, along with his open support of the idea of direct elections, makes him popular among the general public. Yet to take the nomination from Maluf or Andreazza, he will probably have to be willing to match their wheeling and dealing in bidding for the votes of individual PDS delegates.

59. The one key actor who could give Chaves a chance, or possibly tip the nomination to Maluf or Andreazza, is President Figueiredo. If he remains publicly neutral, as he stated he would in December, leaving the battle solely to be decided among PDS politicians in a secret vote, Maluf will probably have the edge. If, however, he declares openly for Chaves, or throws his support to one of the darkhorse candidates who are almost certain to appear in the next few months, Maluf and Andreazza might be stopped. Maluf appears not to stimulate very strong personal loyalties among those who now say they will vote for him, suggesting that his strength could quickly wane if serious doubts developed about his ability to win. **Andreazza's candidacy appeals only to those who want to see the current ruling group, no matter how discredited, remain in power.** To the extent that they believe they will have to answer to their constituents, few politicians would relish this prospect. With regard to Chaves, even though his candidacy might appeal to the average PDS politician, he is unlikely to get the boost he needs from Figueiredo because of the President's unyielding personal antipathy to him.

60. In the end, Figueiredo is not likely to come out strongly for any of the PDS candidates. He dislikes Maluf and Chaves too much to support them openly, and the unacceptability of Andreazza to such a wide spectrum of Brazilians, including many in the military, will probably dissuade him from throwing his reputation behind that candidacy. If the election procedure remains unchanged, therefore, we believe Maluf will win the presidency.

61. The other direction the presidential succession process is most likely to take is the consensus candidate route. Movement toward this solution would probably involve the following kinds of decisions within top political circles:

- Agreement among opposition political parties that direct elections right now are a dead issue and that they could gain significant political strength by having one of their own members named president, even if he entered office without the political clout that would come with a popular mandate.
- Maintenance by Maluf of a decisive edge for the PDS nomination and the decision by a large minority of PDS members that they have more to gain politically by supporting a moderate opposition politician for president than by supporting Maluf.
- Forceful political activity by Figueiredo in favor of an opposition candidate on the grounds that he cannot accept a Maluf victory, and he cannot develop another candidate within the PDS who can beat Maluf.

62. The prospects that the electoral situation will evolve in this direction depend on a number of changes in the status quo and, therefore, it does not have as high a probability as the first scenario. Nonetheless, it is a highly feasible possibility since it does not require any major changes in election rules, and events could drive each of the major political actors to make the necessary decisions to bring it about.

63. At the moment, the opposition politician who would most likely receive the nod as consensus candidate is the present Governor of Minas Gerais, Tancredo Neves. Neves is widely respected in all the places that count: among politicians of all political stripes, by the military and several of the President's top advisers, within business circles, and by the general public. In addition, he has recently strengthened his power within the main opposition party, the Brazilian Democratic Movement (PMDB), and would almost certainly be its choice for president if the PMDB believed it had a chance to win. Vice President Chaves has also recently picked up strength as a possible consensus candidate if he should be denied the PDS nomination. It may be difficult, however, for an opposition political party to nominate him, because he may legally be unable to switch parties this close to the elections.

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64. One set of circumstances that could change the odds to favor the consensus candidate scenario might be new deterioration in Brazilian economic conditions. Particularly if the President were tempted to go to the Congress for new austerity legislation either in order to persuade the banks to release additional tranches from the already approved \$6.5 billion loan or in an effort to seek new loans, he would probably need to increase his bargaining strength to have any chances of success. Certainly, if economic conditions worsen in the next several months, opposition to the government's stabilization program is likely to be so widespread and intense that it would take something as significant as the offer of the presidency to create even the chance of putting together a coalition that would agree to additional sacrifices. [redacted]

65. *Figueiredo's Role.* The main enigma in predicting what turn presidential politics will take in the near future is our inability to know what President Figueiredo will do. Even with the large loss of confidence he has suffered as a leader, the power of the presidency and the cultural predisposition to respond to leadership by the president are so strong that he might be able to exercise decisive influence over the outcome, should he choose to do so. Yet he refuses to take definitive action either to affect the choice of candidate or the choice of electoral process. [redacted]

66. Figueiredo's lack of committed action creates two potential complications for determining how the process will eventually evolve. First, it may delay significant movement toward the consensus-candidate route long enough virtually to foreclose the option, because state governors must resign five months in advance. The individual who has the greatest possibilities of uniting enough of the PDS and the political opposition to beat Maluf in the electoral college, Tancredo Neves, would have to resign as Governor of Minas Gerais by 15 August to be eligible to run. It seems doubtful, however, that he would give up the remaining two and a half years of his governorship to run for president unless he stood a significant chance of winning. That chance may not develop if Figueiredo does not commit himself openly to the consensus-candidate procedure and, probably, to Neves as the best candidate by May at the latest. The other possible consensus candidate, Vice President Chaves, is not required to resign, but he is ineligible to run for president if he serves even one day as acting president in the six months before the election. Consequently, Chaves, too, is thinking of resigning his post by July to

free himself of this constraint. Figueiredo also would probably have to commit himself to an alternative candidate in the PDS by that same period to strengthen the chance of denying Maluf the PDS nomination. [redacted]

67. The second complication that arises [redacted] that by refusing to make an open choice he is inviting groups from all sides to put increasingly heavy pressure on him to decide in their favor. It is impossible to know if Figueiredo would actually resign as President if the politicking around him became too heavy, but that is the one kind of pressure in the past that has led him to talk of resignation. Being subjected to strong criticism and pressure also seem correlated with some of his moments of moodiness, withdrawal, [redacted]

[redacted] If this happened before Chaves resigned to run for the presidency, then the political situation would probably remain relatively stable. Top military leaders in that circumstance would probably support Chaves's accession to the presidency through normal constitutional succession, and the presidential election would be held as scheduled. There is an outside chance, however, that if the removal of Figueiredo or his resignation coincided with a high level of social protests because of a new economic downturn, a Pandora's box of additional possibilities might open. These could range from a short delay in holding the election to a much longer delay and the reimposition of repressive military rule, if military leaders decided that restoring social peace should have the highest priority and could be assured no other way. [redacted]

Impact of Economic Developments on the Presidential Race

68. Up to this point, the course of Brazil's recent economic fortunes has had less influence on developments in presidential succession politics than might have been expected, except to intensify almost everyone's desire to change to a civilian regime. We believe that economic decisionmaking and the outcome of the presidential race will continue largely to be influenced by separate factors unless the economic situation takes an unexpectedly sharp turn for the worse. The choice of method for choosing a president, for example, will be determined most likely by the struggle among

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political elites for advantage, not by pressure from economic elites. The Sao Paulo business community in particular is not likely to lobby in the belief that one method rather than another better serves private-sector interests. Similarly, we do not believe that the most likely unfolding of the economic situation in the next several months—even if Brazil has to return to the international financial community for \$2 billion or so of new money before the end of the year—will particularly boost the chances of one candidate over another. Virtually all of the announced candidates or likely winners are, for example, stressing that Brazil needs to renegotiate its outstanding debt on easier terms if economic recovery is ever to happen. None of them is proposing, or is likely to propose, even a temporary break with the IMF. The rhetoric of any opposition candidate for president will almost certainly be much sharper than that of the PDS candidate in attacking the government's economic performance and the role of the IMF. But the election itself, as long as it is indirect, is more likely to turn on political coalition building than on economic positions.

69. In the much less likely case that popular sentiment in favor of direct elections builds to irresistible proportions, particularly if accompanied by no sign of an economic turnaround or a deepening recession, competition among candidates for party nomination and then for the presidency will be significantly more affected by economic conditions. In such a situation, the candidate who sounds more antigovernment and anti-IMF will benefit. Of the announced candidates in the PDS, Maluf would probably gain an advantage because he can more easily distance himself from the government's economic policymaking than can Chaves and Andreazza, who are members of the government. On the opposition side, a bad turn in the economy accompanied by a move toward direct elections would probably work to the advantage of Ulysses Guimaraes, president of the PMDB, who has been far more outspokenly anti-IMF than has Tancredo Neves. Leonel Brizola would also clearly be helped, in the unlikely case that he were permitted to run.

70. Most of these candidates, if they were running for direct elections in worsening economic circumstances, would probably be sorely tempted to propose that Brazil adopt a temporary and conditional unilateral moratorium on debt repayment as a central part of their platform. Even Brizola, however, would probably not go so far as advocating that Brazil renounce

its debts or break permanently with the IMF. Moreover, any candidate with a serious chance of winning would probably be relatively restrained in his criticism of the United States, because they would all probably perceive the United States as the only actor that might be able to put together an international rescue package for Brazil once they took office.

Outlook and Implications

For Brazil

71. The Brazilian Government is operating within very narrow constraints economically as it attempts to find its way through 1984, trying to avoid having to demand significantly greater sacrifices from the population while simultaneously attempting to satisfy the international financial community. Most of its maneuvering room was probably used up in reaching the most recent 1983 accord with the IMF. If we are correct that the government has neither the clout nor the persuasive powers to tighten austerity further and that it almost certainly will fall short of meeting its 1984 economic goals, then the second half of 1984 is likely to be a period of economic and political turbulence in Brazil. Nonetheless, if economic conditions show steady improvement after the beginning of April—especially the rate of inflation and continued growth in exports—then the turbulence will probably be easily contained even if many of the economic goals are not fully met. The government, for example, will probably be able to loosen import and credit restrictions enough to keep the private sector no worse off than it was in 1983, show enough wage flexibility to prevent widespread strikes, and make enough food available at high but affordable prices to avoid massive deterioration of social conditions in such key areas as Sao Paulo and Rio de Janeiro. Although new money from the IMF and commercial banks and a rescheduling of maturing debt is likely to be necessary before the end of 1984 even under this relatively optimistic scenario, the likelihood that the IMF will be forthcoming as long as the government can demonstrate it made a good effort suggests that enough trade credits and other short-term financing will be available during the year to prevent the economy from being unduly constrained.

72. A significantly worse economic performance by Brazil in 1984 than that presumed by the optimistic scenario would probably lead to a comparably higher level of turmoil in the society. The belief that IMF-prescribed policies do not work would spread and

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become a vocal theme for many groups that now grudgingly accept the necessity of ending government subsidies, restraining wages and credit, and the like. In this situation, the government, under open attack from all sides, would be forced to yield more on austerity than it desires, and it would be under great pressure to take a much harder bargaining stance with the IMF despite its seemingly greater than ever need for IMF support. []

73. Even under these more extreme conditions, however, we doubt that such widespread social violence or civil disobedience would occur as to threaten the basic stability of the society during the time frame of this Estimate. The fundamental values of the political culture, which stress negotiation and compromise over violent change, would take longer to undermine than the months that would remain until the presidential election. The prospects of changing the regime through elections to a civilian-dominated one would also probably continue to appeal to even the most beleaguered groups as the best available way out of the country's dilemma. Moreover, it would most likely still be perceived by the current rulers as an acceptable method of exit by a largely discredited regime, which was standing aside in favor of a new group that might possibly have new answers. []

74. Which one of the leading presidential candidates is actually chosen probably makes very little difference in the way Brazil will be run after the new regime takes office. The election of Maluf, Chaves, or Neves would probably be received with much greater popular acclaim than the elevation of Andreazza since the latter is so tied to the discredited current regime. This would ease Chaves's or Neves's relations with Congress early in their administration, although Maluf—as the PDS nominee—would probably face strong non-PDS congressional political opposition from the beginning. Nonetheless, in terms of what any of the candidates is likely to do, their platforms are very similar and none of the candidates represents a sharp break with tradition. Moreover, as long as the next president is elected indirectly, whoever is chosen will probably have made commitments to existing power groups—such as the military, the political party bosses, and a variety of economic interests (including the state enterprises)—to ensure his election and to reassure them that there will be no drastic or unexpected changes in policy. Without a popular political base from which to draw support, such as the one Argentine President Alfonsin has, any of the indirectly elected

candidates would probably be equally handicapped in taking actions that would significantly reduce the influence or otherwise adversely affect these power brokers after the election. Thus, it is unlikely that any of the candidates, including Vice President Chaves, despite his reputation for honesty, or Tancredo Neves, if the opposition wins with a consensus candidate, would, as president, investigate very rigorously possible human rights abuses by the military, institute corruption proceedings against many former top government officials, or cut back very much the role of the state enterprises in the Brazilian economy. []

75. Their attitudes toward the IMF and Brazil's foreign debt would probably not differ greatly either. Any of them will be under considerable pressure to negotiate much more strenuously with the IMF and the commercial banks than did the present economic team, seeking lower interest rates, a stretched-out grace period, longer maturities, more easily attained performance goals, and the like. If these negotiations go badly, economic nationalism will rise sharply and a temporary delay in interest payments may result, but virtually any president of Brazil over the next year or so will probably continue to try to reach agreement with the IMF rather than take the initiative unilaterally for an indefinite suspension of payments on Brazil's debt. Brazil is simply too in need of imports, trade credits, and export markets for any responsible leader voluntarily to take any other strategy. Since none of the foreseeable choices as president is likely to have even the leeway permitted the present government with respect to pursuing austerity, the really critical decisions on whether Brazil will continue to receive loan money and trade credits in 1985 probably will rest more with the IMF and the bankers than it will with the Brazilian Government. []

76. In the longer term, this lack of freedom of an indirectly elected Brazilian president to take significant new economic initiatives could lead to additional severe disillusionment on the part of the public with the government and its ability to return Brazil to the path of the minimum 4- to 5-percent growth it needs for future stability. Major structural readjustments are needed to reduce the economic weight of government, to hold inflation to tolerable levels, to strengthen the country's ability to earn foreign exchange, and to cut back its dependence on foreign borrowing. Without these adjustments, it will be virtually impossible for Brazil to meet its large debt servicing requirements in the mid-1980s as loan repayments contracted in the

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early 1980s come due. In fact, even with most of these readjustments, Brazil will probably be unable to both pay back its loans and begin to grow again unless *either* the international economic environment remains extremely favorable for the next five years or so *or* the Brazilian debt is regularly renegotiated during this period in order to lighten the debt burden and provide the resource margin for growth. Another world economic slump or round of tight money policies in the industrialized countries would probably frustrate even Brazil's best readjustment efforts, raising a question as to whether Brazil could pull out of economic recession even with a restructuring of debt.

77. If the worst happens and the new president either cannot bring about the necessary structural changes or world economic conditions defeat Brazil's best efforts, then questions about the country's long-term stability will probably arise. Brazil has remaining one option, however, that might at least delay a downward spiral into widespread political violence and social breakdown on the one hand, or a reimposition of authoritarian military rule, on the other: direct, popular elections for a new president. Right now the appeal of direct elections is very strong to a public looking for a leader who can galvanize the society and restore the presidency to its traditionally powerful, highly respected function. Even under relatively favorable circumstances, there will be many pressures on any indirectly elected president to permit a constitutional revision that will cut short his six-year term in favor of a new, directly elected president. If economic conditions do not substantially improve by the end of 1985, these pressures will probably become almost irresistible.

For US-Brazilian Relations

78. In the last decade or so, the state of US relations with Brazil seems to have been a product more of Brazilian perceptions of the respect with which the United States is treating Brazil than it is of the current level of economic well-being or distress. Relations reached their lowest point in years in 1977, for example, despite the relatively good private-sector commercial and financial relations that existed at that point, because Brazil felt the US Government was attempting to dictate to it on nuclear and human rights matters. On the other hand, relations have steadily improved over the last two years or so even as Brazil's association with the US-dominated interna-

tional financial community has become increasingly difficult. This has occurred because Brazilian leaders believe the US Government has made a concerted effort to improve the level of information the two governments exchange across a broad range of subjects, has approached Brazil as an equal in attempting to solve problems, and is understanding of its need to differ with the United States on some foreign policy issues in areas such as the Middle East. The Brazilian Government (and many in the private sector) also perceives the US Government as essentially an ally at this point in its attempts to negotiate debt relief, obtain new money, and, despite numerous commercial frictions, expand exports. (s

79. Continuation of this trend toward frank, but generally good, relations depends on whether these perceptions continue to hold. Even if negotiations with the IMF and the commercial banks become more strenuous later in 1984, we believe the chances are good that relations will continue on their upward course as long as the Brazilians believe the US Government is doing its best to contain protectionist pressures in the United States, is encouraging the IMF and banks to be as forthcoming with Brazil as possible, and is not attempting to urge on Brazil any strategic relationships or joint actions that would tend to compromise its independent foreign policy. As the Brazilian military returns to focus primarily on professional pursuits, we believe the opportunities for strengthening relations with it will be especially good if the United States can respond to its professionalization needs without pressuring it in a way that would arouse its easily stimulated nationalistic sentiments.

80. Relations in the nuclear area are in a delicate balance. There has been some improvement over the last two years or so as the United States has become less concerned that Brazil represents a near-term proliferation threat.

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81. The one area where Brazilian-US relations could most likely become more strained over the course of the next year or so involves Brazil's continued need for IMF support, even if its economic performance falls noticeably short of meeting IMF goals. If this happens before the election, Brazil will

expect the United States to do everything it can to keep the economy afloat until the new Brazilian president has taken office. After the election, there will probably be increased pressure on the United States to support Brazilian requests for a major restructuring of Brazil's debt. These pressures will become very insistent if Brazil fails to recover economically because of such external events as a rise in interest rates or oil prices, or insufficient expansion of markets in the United States for Brazilian goods. [REDACTED]

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ANNEX A

FIGUEIREDO'S PROBLEMS IN MORE DETAIL

1. The administration of President Figueiredo has suffered a major loss of credibility with the Brazilian people over the last three years or so. Underlying this loss are three fundamental weaknesses that would be key vulnerabilities to any bureaucratic authoritarian political regime but which are especially damaging to the governing capabilities of the Figueiredo regime. In brief, the ability of the regime to rule effectively is being undercut by a sharp drop in available resources, weak leadership from the President and his principal lieutenants, and an unresponsive bureaucracy.

Declining Resources

2. For the last three years, the Brazilian economy has been in decline, sharply limiting the resources available to the Figueiredo administration and undermining public confidence in its ability to govern at home and to improve Brazil's international status. Gross domestic product fell about 3.5 percent in 1981, stagnated in 1982, and fell approximately another 5 percent in 1983. These are the first years of negative GDP growth since the Brazilians began to keep national income accounts in 1947. Per capita GDP also dropped in all three years. Inflation, on the other hand, was close to 100 percent in 1981 and 1982, and rose to a little over 200 percent in 1983. Unemployment and underemployment also climbed during this period to what are probably close to historical highs; by the end of 1983 an estimated 25 percent of the labor force was affected. Government surveys have shown that real wages dropped in 1982 and 1983, confirming public belief that, for the first time since the Brazilian economic "miracle" began in 1968, general living standards have declined.

3. Brazil's international economic standing has also suffered in the last two years. Particularly damaging to the Figueiredo government, especially in terms of projecting the image of Brazil as a country in charge of its own destiny, was the need to have recourse to the International Monetary Fund (IMF) in 1982. By that point, Brazil simply could not earn enough through exports to pay its mounting international bills. In addition, turmoil in international financial markets had caused sources of new financing virtually to disappear, and Brazil's foreign reserves were dropping

dangerously low. Weighed down by \$80 billion in foreign debt, Brazil applied for a loan from the IMF in December 1982. While the action came as no surprise to the Brazilian public, because it was the logical result of the 1981-82 financial crisis, it nonetheless was perceived as something of a national humiliation. Brazilian governments, civilian and military alike, had made a point of denying Brazil would ever submit itself to the conditions imposed by the IMF for access to its money ever since President Kubitschek had broken off negotiations for an IMF loan in 1957.

4. Brazil's relations with the IMF and commercial banks were very uncertain throughout 1983 as the government's inability to achieve certain internal economic goals consistent with its agreement with the IMF caused the IMF to suspend disbursement of the loan funds and required revising the Brazil-IMF agreement twice. Both of the revisions created an additional anti-IMF backlash among many political and business sectors in Brazil, even among some politicians who ostensibly are supporters of the government. Calls for a unilateral moratorium on debt repayment were heard from some of these sectors and, in fact, Brazil had accumulated \$2-3 billion in interest payment arrearages by the end of 1983. A crisis with US banks was avoided only by frantic last-minute negotiations with the IMF and banks, which secured enough money to pay off those arrearages that would have been more than 90 days overdue by 31 December. A new loan package of \$6.5 billion negotiated with the IMF and Brazil's commercial creditors has secured a large part of the external financing Brazil will need for 1984, but continued access to this money may require further tough domestic austerity measures, which the Brazilian public will be increasingly loath to accept if domestic economic conditions—such as the rate of inflation—do not soon show signs of improvement.

Leadership

5. As long as Brazil was prospering economically, as it did in the mid-to-late 1970s, most foreign and domestic observers believed that national policy was in the hands of competent leaders. Even after growth rates began to drop off and inflation picked up in the

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aftermath of the first oil price shock in 1973, concern about the quality of leaders in the Brazilian Government was not widely expressed. In retrospect, fundamental doubts about the ability of the military and especially the technocrats who make and implement Brazilian policy probably really began to grow only in 1980-81, a year or so after President Figueiredo took office. The first major blow to the Brazilians' confidence in the ability of their leaders to move the country forward on the path to *grandeza* occurred in reaction to the evident failure of Minister of Planning Delfim Netto to adapt Brazilian economic policies successfully to the consequences of the second oil price shock of 1979. Delfim had the reputation of a "miracle maker," stemming from his days as economic czar when Brazil was achieving double-digit growth in 1968-74. His attempt to correct Brazil's declining economic fortunes in 1980 by applying the same expansionist policies that had worked well during the earlier period, followed by a sharp swing to austerity policies in 1981 that were applied in an uncertain and vacillating fashion, brought widespread disillusionment about whether technocrats knew what they were doing. These growing concerns were probably accelerated by the abrupt departure from government of General (Ret.) Golbery do Couto e Silva in August 1981. Golbery had served as top political adviser to President Castello Branco (1964-67) and to Figueiredo's predecessor, President Ernesto Geisel (1974-79), and was generally considered one of the strongest forces in government for a continued, if measured, opening (*abertura*) of the political system that would lead eventually to a return to civilian control. His resignation because of policy differences with Delfim and with another close presidential adviser, General Octavio Aguiar de Medeiros, Chief of the National Intelligence Service (SNI), stimulated public doubts about the government's political astuteness and the sincerity of its commitment to *abertura*. [redacted]

6. The final decline in the government's credibility and public confidence in Brazil's leaders took place following Figueiredo's return to office in August 1983 after a six-week absence because of heart surgery. Figueiredo had enjoyed wide popularity during his first years in office, primarily because of public appreciation of his clear commitment to carrying out the process of political liberalization. By the fall of 1982, however, two years of recession had considerably eroded his popularity and public perceptions of his leadership ability. These doubts were exacerbated in mid-1983 as reports began to circulate (and were

played up in the press) that mounting criticism and the strain of coping with seemingly intractable problems were adversely affecting Figueiredo's health and state of mind. [redacted]

7. At this point, the public and almost all important elites have lost confidence that Brasilia knows what it is doing or that anyone in the government has a vision of how to lead the country out of its present difficulties. On the economic side, decisionmaking at the top and down through the bureaucracy has degenerated into day-to-day attempts to cope with immediate problems, hesitation to take responsibility to make difficult decisions, and general drift and vacillation. On the political side, the President has clearly lost control over his own political party and the ability to impose his successor. [redacted]

8. One of the prerogatives that Figueiredo thought he was acquiring when he accepted the presidency in 1979 was the power to choose—or at least have the lead role in choosing—the next president as his two most recent predecessors had done. The first signs that his control over this process might be threatened appeared in 1982, as it became apparent that the progovernment Social Democratic Party (PDS), as a result of the November legislative elections, might lose its majority in the federal congress, the institution which heretofore had functioned as an electoral college to ratify previous military presidents' choices of successor. To obviate this problem, the government quickly brought about constitutional changes that added electors to the electoral college from the state assemblies, thereby restoring the PDS's majority because it was almost certain to retain control of the state legislatures. [redacted]

9. This strategy worked insofar as the PDS now has a 358-to-328 voting edge in the electoral college. What

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Figueiredo and his advisers had not foreseen, however, was that Paulo Maluf, a newly elected PDS federal deputy from Sao Paulo, would not wait for Figueiredo's nod as his choice for the presidency. Instead, Maluf began immediately a well-funded and highly professional campaign to lock up as many PDS electoral votes as he could so that he could win the PDS nomination for president regardless of whatever preference Figueiredo might eventually announce. Perhaps in part because of this effrontery, Figueiredo has let it be known he is totally opposed to Maluf. Yet, his failure to indicate who is his preferred candidate or to use the immense patronage and other powers of the presidency to stop Maluf have essentially taken the control from him.

The Bureaucracy

10. Of the three central problems the Figueiredo government faces, the one it is probably least responsible for is the public perception that the civil bureaucracy has developed such power and independence that it is largely out of control. This criticism is most often directed against the state-owned enterprises or "parastatals." At the popular level, the state enterprises are seen as baronies, led in many cases by retired military officers who have gained vast wealth while heading these companies. The media frequently play up the perquisites (large cars, expensive trips, lavish parties) customarily accompanying these positions, claiming that the state enterprise officials are flaunting these status symbols even as the rest of society is having to tighten belts because of recession and austerity.

11. At a more fundamental level, the autonomous behavior of the state enterprise is, in fact, a major complicating factor in Brazil's effort to overcome its current economic difficulties. The role of the state enterprise in Brazil is greater than in any other Latin American country. The top 23 Brazilian firms—and 84 of the top 200—are parastatals. As a group, they account for 33 percent of GDP, 60 percent of domestic investment, and 40 percent of nonoil imports. They employ close to 1.5 million people, including 14,000 to 15,000 former military officers.

12. The state enterprises have played a crucial role in the economic development of Brazil, often taking

on projects that were too large for the private sector to handle or not sufficiently attractive as investment risks. They have been particularly suited to taking on the immense developmental tasks associated with the military's attempt to harness Brazil's great natural resources in its drive toward *grandeza*. As long as Brazil's economy was expanding rapidly, they were very appropriate engines of change. Because of the momentum they developed, however, in favor of gigantic expenditures of money and human resources to solve problems, they have been very slow to adapt to a constricting economy. In 1981 and 1982, for example, as the overall economy shrank, the expenditures of the state enterprises grew by 2.5 and 11 percent, respectively. Their deficits—4.2 percent of GDP in 1981 and 5 percent in 1982—became major sources of inflationary pressure. Their preferential access to domestic credit markets crowded out private enterprise as credit availability shrank, and their heavy foreign borrowing—their share of the foreign debt rose from 60 in 1977 to almost 70 percent in 1980—contributed substantially to Brazil's indebtedness. The state enterprises also continued to hire new personnel during most of the last three years, long after the employee rosters of the rest of the economy began to drop as part of austerity.

13. Figueiredo entered office in 1979 promising to reduce the federal government's role in the economy. His administration subsequently targeted the state enterprises, which he and his advisers believed had become so large and powerful that the cumulative effect of their activities could undermine overall economic policy. As part of that effort, Figueiredo in 1979 created the Secretariat for the Control of State Enterprises (SEST) under the Planning Ministry. The new agency was charged with setting limits on the parastatals' foreign borrowing, spending, imports, and prices for goods and services. SEST has had some marginal impact. For the first time a consolidated budget for all the state enterprises was created, and twice last year a series of new budget cuts—particularly in investment—were ordered. Nonetheless, the influence of especially the largest of the state enterprises is such, and their role in the economy is so well entrenched, that they are often able to avoid mandated restrictions. In general, they have been able to maintain their operations and personnel rosters, avoid sharp reductions of their official investment budgets, and protect their basic equities.

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ANNEX B

THE POLITICAL ACTORS

1. At present the number of groups with significant national political influence is quite limited. The ruling elite today essentially consists of the President and his closest technocratic, military, and political advisers, and a small group of politicians with whom the executive must now negotiate to assure passage of legislation. []

2. Most other groups, including the bulk of the military and businessmen, are basically bystanders in the political process. As the system continues to open, however, these groups and others possibly representing the middle class could become more active politically. []

The Ruling Elite

3. As long as Brazil had a strong president, the focus of power within the system was centered on him and his closest advisers. In the past, the latter usually included the heads of the president's civilian and military households; the Army (preeminent), Navy, and Air Force ministers; the head of the National Intelligence Service (SNI), and the economic czar (usually the minister of planning). The Army high command (all the four-star generals) also exerted major influence, especially on matters touching on (broadly defined) national security when they acted to protect the military's institutional interests. The technocrats were given considerable latitude to run the day-to-day business of government, but, with the exception of the economic czar, they did not often originate major policies and their initiatives were usually subject to veto by the military. Businessmen similarly did not often inspire new policy, but their interests and those of the government were generally in harmony, and they had frequent and easy recourse to the sources of power when they had a complaint. Progovernment politicians were tolerated (as was an official opposition party) and were expected to pass whatever legislation was called for by the executive. []

4. The group that rules today no longer contains, even as junior partners, the industrialists and business entrepreneurs. In addition, the military high command has retreated considerably from its previous policy role and attempts much less often to exert

institutional influence. Most of the politically relevant statements now emanating from the generals emphasize their desire to remove the military from politics, returning it entirely to professional military pursuits. []

5. The relationship among those who remain in the ruling group—the president and his advisers, the technocrats, and progovernment politicians—has changed quite sharply. Decisionmaking power, for example, is much more fragmented. Technocrats manning the ministries and the state enterprises now represent, after 20 years of growth and accumulation of resources, a separate power base, no longer directly dependent on the military for their positions and their authority. The politicians, as an outcome of the gradual transition back toward civilian rule, have also acquired separate interests and an independent political base now that they have popular constituencies to represent and to answer to. At this stage in the political transition process, there is no center of gravity: the military is withdrawing from politics, the bureaucracy is strong enough to protect itself from outside control but does not have the power of initiative, and the politicians are powerful enough to interfere with the wishes of the executive branch but not yet strong or well organized enough to impose their authority. []

6. Normally, a Brazilian president could exercise sufficient leadership to cope with even this amount of confusion if he exercised the power available to him. []

[] He has, for example, left much of the daily chores of running the Office of the Presidency to his SNI chief, General Octavio Aguiar de Medeiros, most dealings with politicians and the Congress to head of the civilian household Leitao de Abreu, and virtually all economic decisionmaking to Planning Minister Delfim Netto. The two problems with this arrangement are that the three advisers do not trust each other and have difficulty coordinating actions, and that Figueiredo's relations with Leitao de Abreu and Medeiros are increasingly poor. The growing bitterness between Figueiredo and Medeiros is particularly important, because it has eliminated the possibility that Medeiros

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might be chosen as Figueiredo's presidential nominee, a very strong likelihood two years ago. The distance between the two has also reduced the influence of the SNI as an institution, especially in terms of the policy recommendations the SNI had been accustomed to having accepted by previous military presidents. Figueiredo is also estranged from Vice President Chaves.

7. The result of this disarray within the ruling group has been a drop in the predictability of the decisions the political system yields, concerning both the likely duration and consequences of decrees issued by the executive branch and the probable content of legislation passed by the Congress. The extent of the existing uncertainty is highlighted by the struggle that took place recently while establishing a wage law that was austere enough to satisfy the IMF:

- The executive branch had to issue three executive decrees with progressively softened provisions on how much wages could be permitted to rise in relation to past inflation before it arrived at one that could be used as the basis for successful negotiations with Congress.
- The leader of the federal Chamber of Deputies, a member of the progovernment PDS, was instrumental in preventing the executive from using a particular parliamentary strategy for passing the first version of the decree law when it became clear it would not pass on its own merits.
- For the first time since the beginning of military rule, the President was forced into real negotiations with politicians to obtain passage of crucial legislation.
- Even now that a wage bill has been passed, uncertainty reigns as to whether its provisions for not permitting wage raises, on the average, to increase faster than inflation will be applied equally to the private and public sectors or will be used primarily to attempt to bring down the latter's wages. In any case, there is considerable doubt that the government will attempt strenuously to enforce the wage-limiting provisions.

The Political Class

8. The prospects and influence of professional politicians have revived strongly enough in the last year or so to be thought of, after 20 years in the wilderness, as

significant political actors. Since the November 1982 congressional elections, when opposition parties won a majority in the federal Chamber of Deputies, the government has learned, albeit slowly and often reluctantly, that it must treat politicians as serious participants in the governing process, even though political parties and the Congress itself remain fairly weak political institutions that can be manipulated by strong and determined presidents.

9. Historically, political parties in Brazil have been artificial, top-down creations, often established primarily to promote the fortunes of individual politicians. Ideology is usually of minimal importance in understanding the positions the parties are likely to take on issues. They often group quite diverse interests, tend to enter into and leave coalitions easily on different issues, and, partly because of their lack of ideological fervor, take relatively moderate rather than extremist stands. Their memberships are also frequently fractious, and parties usually are composed of subgroups that often are in combat with their own leadership. The Brazilian Congress traditionally reflects these weaknesses, generally finding it difficult to find enough common ground and strength of conviction to develop its own initiatives against a purposeful president.

10. Current Brazilian political parties and the Congress have these same weaknesses. Nonetheless, partly because they have been powerless for so long and partly because they are riding a wave of tremendous popular sentiment in favor of restoring civilian rule, they are successfully demanding a larger role in the political process. Some of their energies are consumed by strong rhetoric focused on attacking the government's economic team and the disastrous effect its policies are having on the well-being of the middle class and poor. The opposition parties have, for example, passed a nonbinding resolution decrying the IMF austerity program and advocating a break in relations with the IMF. These activities, while they contribute to the perception that the government is beleaguered, do not seriously affect relations between the administration and Congress.

11. Although the five political parties represented in the federal Chamber of Deputies ostensibly divide between 235 members of the progovernment PDS, and 244 members of four opposition parties, this distinction blurs in practice. The administration frequently finds that it must negotiate at least as vigorously with the leaders of the PDS to achieve passage of

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needed legislation as it does with leaders of the opposition, because congressional members of all political stripes have developed institutional loyalties to the Congress that take priority over party differences when, in struggles with the executive branch, they feel their prerogatives as legislators are being ignored.

12. Lines between the parties blur also because ideological divisions among them are so imprecise. Both major parties, but particularly the principal opposition, the Brazilian Democratic Movement Party (PMDB), are extremely heterogeneous groupings. The PMDB, for example, runs a long ideological gamut from a private-enterprise-oriented right to a Marxist left. The PDS, while somewhat less diverse ideologically, is split between a majority that tends to support the government and a large minority (the "participationists") who are as critical of the administration's economic policies as are many in the formal opposition.

13. Of the three small parties, the most significant is the prolabor Brazilian Labor Party (PTB), which has enough votes to provide the government with a majority in the Chamber of Deputies when it can hold the PDS in line. PTB deputies are not committed to any particular political philosophy and, as was demonstrated in passing the government's wage bill in November, can sometimes be won over with appropriate patronage offers. In that case, they agreed to vote with the government in exchange for the promise that one of their members would be named to head a ministry, an offer that the PDS has not yet achieved despite its standing as the ostensible progovernment party.

The Military

14. For most of the last two decades, military officers have generally believed their institutional interests were virtually identical with those of the government. In particular, it was basic doctrine that Brazil needed rapid economic development and respite from civilian politics in order to stave off threats from domestic leftist forces (possibly abetted by Cuba and the Soviet Union) and to make a serious effort to attain major power status by the end of the century. The primary role of the military, in this situation, was to occupy many of the main governmental decision-making offices, to provide support for civilian technocrats to apply their developmental policies free from political challenge, and to maintain firm hierarchical discipline in support of the president and his advisers.

15. Senior officers have become increasingly disturbed by the government's lack of direction and, particularly, Figueiredo's failure to provide leadership during these last several months of increasing economic troubles and political uncertainty. They fear that the military will be more and more blamed for the country's problems, thereby further damaging its reputation in the eyes of the public. Stimulated by events in Argentina, they are also concerned with rising popular reaction against corruption in government, some of which is directed at those military officials who hold office in the ministries and state enterprises. This concern about corruption extends down through the ranks, with some middle- and junior-grade officers beginning to worry about the effects on their careers of loss of public esteem for the military.

16. The stress of being targets of public criticism is creating some dissension within the military. Virtually all officers continue to support continued political liberalization and to return to civilian rule because they see that avenue as the only way the military can regain its professional orientation. Nonetheless, differences of opinion have developed within the Army over how to evaluate Figueiredo's performance as President. Some believe he has been a disaster and that it was a mistake to elect him to the office. Others believe he has done as well as could be expected under difficult circumstances. Some Air Force and Navy officers are bitter toward the Army, agreeing with opposition politicians that postrevolution governments, led by Army officers, have committed huge blunders that have caused the country to lose some of its economic sovereignty and the military some of its honor. Junior officers of all services are unhappy with their senior leaders, who appear to be adrift in the current economic crisis, who may be involved in corruption themselves, and who are not speaking out forcefully to defend the military from what these officers feel is often unfair criticism.

17. Despite these signs of internal division, the Brazilian military high command remains loyal to Figueiredo, and hierarchical discipline within the ranks is strong. Unlike in earlier years, there are virtually no "hardline" officers left in the higher ranks around whom disgruntled officers can rally since, through skillful use of the promotion process, Figueiredo and Army Minister Pires have rewarded loyalty and removed potential dissidents. A few retired officers have spoken in terms of possibly removing Figueiredo, but at this point they have virtually no influence

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[redacted] In addition, the one active-duty senior officer that dissident military personnel might have rallied around, General Newton do Oliveira Cruz, head of the Brasilia military command and former chief of the SNI in Rio de Janeiro, is on the verge of being removed from his command and forcibly retired by the Army Minister because of a public temper tantrum with the media that embarrassed the Army. [redacted]

The Business Community

18. Brazilian businessmen, now suffering through their fourth year of recession, are massively unhappy with the Figueiredo administration. Much of the discontent is the natural outgrowth of bad business times after many years of expanding markets and high profits, and probably would have been directed at any government that had to adopt austerity policies to combat high inflation and a severe balance-of-payments crunch. Antiadministration feelings, already high because of business perceptions of inept economic decisionmaking and execution by the government, have been exacerbated by businessmen's belief that Delfim has failed to demand—or at least negotiate strenuously for—more lenient conditions on IMF and commercial bank loans and, in particular, that Delfim has treated the business community in a cavalier way. In their view, Brasilia has moved from one stopgap austerity measure to another in a largely unsuccessful effort to combat recession. These frequent shifts in policy have disrupted business planning, and a wide array of unevenly applied government regulations has made day-to-day business operations exceedingly difficult. Most important, private businessmen generally (including the potentially powerful industrialists of Sao Paulo) believe they have little of the influence with Figueiredo and his ministers that they had, and believed they deserved because of their general support of military rule, with previous administrations. In particular, they believe the costs of austerity have been placed much more heavily on the private sector than on the many businesses run by the government. They perceive, quite accurately, that they have had to absorb much more unemployment, squeeze on profits, and cuts in investment capital, for example, than have state enterprises. In addition, they have come last in terms of access to credit and to foreign exchange with which to pay their import bills [redacted]

19. In the last few months, whatever support there might have once existed in the business community for

the IMF austerity program has largely dissipated. There is a widespread belief that the program sets unobtainable goals, will be counterproductive in that it will inhibit industrial production (and thus exports), and does not attack what private-sector businessmen consider the key structural barrier to a return to economic growth: the size of the public-sector deficit. Many industrialists and other entrepreneurs fervently believe that no government program to bring back even modest growth rates can succeed unless spending by state enterprises is brought under control on the domestic side and, internationally, the Brazilian foreign debt is restructured. [redacted]

20. Up to now, business unhappiness has been reflected more in rhetoric than it has in political activity. In August 1983 a group of leading Sao Paulo industrialists did release an unusual public letter denouncing the harsh antirecession actions demanded by the IMF and acquiesced in by the government, and they urged Brasilia to counter the recession instead by stimulating consumer demand. In addition, some of the congressional opposition to earlier versions of the government-sponsored wage bill was undoubtedly sparked by business constituents. Nonetheless, the Sao Paulo State Federation of Industries, which is by far the best organized and most influential business organization in Brazil, has not developed its own comprehensive program for combating the recession, argued in favor of any of its own members as possible substitutes for the current economic team, or tried to organize a united front to boost a presidential candidate sympathetic to private-sector interests. [redacted]

The Other Bystanders

Labor

21. From time to time, organized labor, which represents only one-fifth of all Brazilian workers, gives the appearance of a force ready to break out of its historically weak position and to exert more influence nationally, both on bread-and-butter labor issues and as a national political actor. In 1979-80, for example, as the political system began to open and the government became more tolerant of the potentially disruptive activity, workers struck successfully in record numbers for higher wages and better working conditions. By 1981 the level of union activism and rhetoric had escalated to the point that labor leaders were meeting to attempt to organize a single national labor confederation, and a prominent former union chief, Luis Inacio da Silva (better known as "Lula"), was in

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the midst of organizing Brazil's first grassroots labor party, the Worker's Party (PT) []

22. These efforts were not without results. A new wage law promulgated by Brasilia in November 1979, which considerably liberalized wage readjustments, undoubtedly was partially stimulated by government desires to restore labor peace. And Lula, using the PT as his political base, ran for governor of Sao Paulo in the November 1982 elections. Nonetheless, later events were to demonstrate that organized labor's basic weaknesses—the inability of its leaders to galvanize workers behind common goals, fractiousness among these leaders, and the subservience of unions to the government—have not changed. With regard to strike activity, for example, despite the decline in real wages, workers have become increasingly reluctant to risk their jobs by threatening walkouts as unemployment has continued to rise. The hesitant steps toward labor unity, moreover, have faltered as union leaders have split into two groups, each attempting to create competing national labor confederations. On the political side, Lula's run for governor was a failure. He received only 10 percent of the votes cast and could not even carry some Sao Paulo industrial areas where PT-affiliated unions were supposed to be strong. Nationally, the PT did elect eight federal deputies (six from Sao Paulo), but it showed little strength outside its home state. At present, its strength does not seem to be growing, a trend which, if it continues, will eliminate the PT as a political party after the next congressional elections. According to current electoral rules, all parties must poll at least 3 percent of the total vote in a minimum of nine separate states in the next election to retain their registration. The PT reached that floor in only three states in 1982. []

23. The main barrier to the evolution of organized labor into an autonomous political actor is the extent to which it is controlled by the government. Legislation passed in the 1930s, which remains basically in force today, prescribes the structure of union organization and the permissible scope of labor's political and economic activities. The government controls the labor system through a large, permanent bureaucracy which monitors union activities and has the power to discipline and even remove union leaders for "illegal" acts. In addition, the bulk of union funds come from the government, and only state-approved unions receive this money. Most important, the rank and file accept this patron-client association as the proper relationship between government and labor, and there is little sentiment in favor of changing it drastically. []

The Middle Class

24. Rapid economic growth in the late 1960s and 1970s has created a large and increasingly influential middle class which, until the last two years or so, provided much of the political base for the military/technocratic regime. This group is estimated to number some 25-30 million people, or about 20 percent of the population. Mostly employed in services and industry, the middle class receives more than one-third of the country's personal income and accounts for most consumer spending. []

25. The middle class has been hit particularly hard by recession and by the government's austerity policies. The government's wage policy since 1979, which has focused on restricting cost-of-living increases for those in the middle and upper salary brackets at a time of accelerating inflation, has caused a significant loss of income. They could lose another 20 to 30 percent of their ostensible purchasing power during the next year if the rate of price increases, which reached more than 200 percent in 1983, does not decline substantially. A continued rise in unemployment and underemployment among the middle class is also likely in those circumstances. []

26. The economic frustration of this group has already had clear, though limited, political repercussions. It undoubtedly played a significant role in the November 1982 elections, when middle-income voters shifted in large numbers to the opposition. These votes, combined with those of less privileged groups, enabled opposition parties to gain control of Brazil's wealthiest and most populous states. The discontent of these constituents also probably contributed to divisions in the PDS and the assertiveness of opposition parties as they resisted initial government efforts in the fall of 1983 to pass the new wage-restraint legislation. Direct economic protests by the middle class have also become more frequent. In May and June 1983, many homeowners threatened not to pay rising mortgage payments, and more than 100,000 civil servants struck for higher pay and job security. Thousands of state-enterprise employees—mostly middle-class and well-paid—demonstrated against cuts in budgets and compensation. []

27. Two other major concerns of the middle class are the rise in crime experienced in most cities in the last year or so, but particularly in Rio de Janeiro and Sao Paulo, and escalating corruption. Informal polls conducted by the media indicate that almost everyone

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interviewed has been or knows someone who has been robbed. With regard to corruption, many people feel it has reached intolerable proportions. In part, this is due to a perception that those military officials who participate in government have become tainted, an image which conflicts directly with that which the military helped spread when it entered power in 1964—that it is a cleansing or moralizing force with the duty of combating such influences in society. In part, the reaction against corruption has also been caused by its perceived magnitude and pervasiveness. There is a general belief that no one in the public bureaucracy will do anything without a bribe. This becomes particularly difficult to accept as disposable income shrinks faster for those in the private sector than for those employed by the government.

28. Considering the strength of middle-class grievances against the government, what is perhaps most noteworthy has been the relatively restrained political consequences so far of their unhappiness. To a degree, the government has diverted part of the anger by making small, even if completely inadequate, gestures in the direction of dealing with some of the problems. The governments of Sao Paulo and Rio, for example, have increased police patrols in the better parts of towns and have made big media events out of the delivery of small amounts of already ordered police equipment. Much more important, however, is the fact that middle-class Brazilians, even when their rising expectations are being frustrated, tend to focus their energies more on finding private ways to cope with the situation than on organizing public ways to change policies or officials. The reaction of middle-income families to economic distress, for example, has focused primarily on cutting cash expenses (often through participation in the rapidly expanding underground barter economy), generating additional income through employment of more family members or finding second or even third jobs for the main breadwinner, and searching out ingenious ways of beating the system—such as discovering pretexts for withdrawing forced savings from the National Housing Bank.

The Extreme Left

29. By almost any standards, the extreme left in Brazil is remarkably small and weak considering the fertile ground for its activities that might be thought to exist because of the widespread and growing economic discontent. The majority of Brazilians, for example—

some 80-90 million or about 65 percent of the population—are impoverished and have been growing more so in the last three years. Their ranks have been swelled by some who had reached the lower ranks of the middle class and now, usually because of unemployment, have fallen back into the lower income group. Price hikes—particularly for food, which increased some 300 percent nationwide in 1983—have especially hurt the poor. According to the Brazilian press, the minimum wage will not buy enough food for even one adult at current prices.

30. Despite their growing economic problems, however, the poor, for the most part, remain unavailable to the radical left. They are generally difficult to organize for any purpose—even in the urban slums, unlike in several other Latin American countries. Rather than being attracted to leftist values and causes, most of the poor are more interested in just surviving—or, for those at the top of the lower income spectrum, in aspiring to middle-class status—than they are in taking to the streets to agitate against the government.

31. The foodstore lootings in April and again in September and October 1983 raised the possibility that the poor might be becoming more volatile. These lootings, however, were generally not accompanied by violence, were fairly isolated and contained by the authorities, and probably acted more as a safety valve for hungry people (particularly since the police did not overreact) than they did as a harbinger of more widespread violence to come.

32. Even if the poor (and the disappointed middle class) were more susceptible to leftist appeals, the radical left in Brazil is not in a position to take advantage of growing economic and social discontent. The one possible leader on the left who might have national appeal is Leonel Brizola, the Governor of Rio de Janeiro. Brizola, ex-President Goulart's brother-in-law and a former radical leftist who had his political rights canceled in 1964, climaxed a remarkable comeback by winning the governorship in the November 1982 elections with widespread popular support. Since that time, his image as an effective leader has suffered, however. Polls indicate that many people in Rio de Janeiro, even in the lower classes where he was strongest, believe he has been a very poor governor. In addition, he has alienated many on the left by his refusal to speak out against the Figueiredo administration (which he depends on for the resources to run his state) and by the way he has maneuvered in state

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politics, seeking votes from the center in the state legislature at the cost of his old-line, leftist supporters. Brizola's strategy is to build support in the center-left, hoping that he can run for president whenever direct elections are held. Most military officers remain strongly opposed to this prospect, however, and Brizola has made no progress in developing a national political base or in raising the money he would need for a national campaign.

Opinions in Brazil are divided as to whether Brizola could use national television to make a charismatic appeal to the lower and middle classes that would sweep him into office in a direct election. The fear that this could happen is enough, we believe, to assure that the military would not permit him to run any time soon if, somehow, direct elections come about.

33. The other groups on the radical left are in even worse shape. They all suffer from three main problems:

- The government's program of political liberalization has taken away from them the antiauthoritarian issue on which the government might have been most vulnerable.
- State dominance over the Brazilian economy is so extensive that there is little room on the left to agitate for greater socialist control.
- They are so racked with internal dissent and penetrated by government security and intelligence organizations that it would be very difficult for any of them to pose a serious threat.

34. The largest of the groups on the extreme left, the Moscow-line Brazilian Communist Party (PCB), is estimated to have fewer than 10,000 members; it probably has considerably fewer activists. In recent years, the PCB not only has formally eschewed violent antigovernment activity, but has actually become a force for moderation with those groups, such as organized labor and students, where it has some influence. It is now pouring all its efforts into a campaign to persuade the government to permit registration of the PCB as a legal political party. Because it fears government repression should it step out of line and that opposition political parties, such as the PMDB, would withdraw support of its legalization campaign, it has cautioned leftist allies against attempting to call a

general labor strike or a national student strike or to sponsor civil disturbances. Its strategy is to play for the much longer term, hoping that a return to civilian rule will eventually allow it greater freedom of action.

35. Internal dissension and tight surveillance by the government's security and intelligence organizations also diminish the PCB's potential as a political force. As recently as August 1983, for example, 11 members of the Sao Paulo State Central Committee were expelled from the PCB for opposing the legalization campaign. And earlier, in December 1982, the Brazilian Federal Police raided the Seventh Congress of the PCB, arresting many members of the national Central Committee.

36. Other extreme left groups are not prospering either. The Communist Party of Brazil (PC do B), a Trotskyite (formerly Maoist) splinter group, consists of a few hundred members and has survived only in Sao Paulo. It attempted to exploit a wave of street riots and foodstore looting in Sao Paulo in April 1983, but it could claim no credit for provoking them. A third group, the 8 October Revolutionary Movement (MR-8), is also barely alive. After attempting unsuccessfully to run three candidates for election in the November 1982 race, it split into three groups. One joined the PMDB shortly after the election, and the second rejoined the PCB in July 1983. A third faction of 200 to 300 remains active in Sao Paulo and is attempting, without much success, to become influential in the popular movement for direct elections.

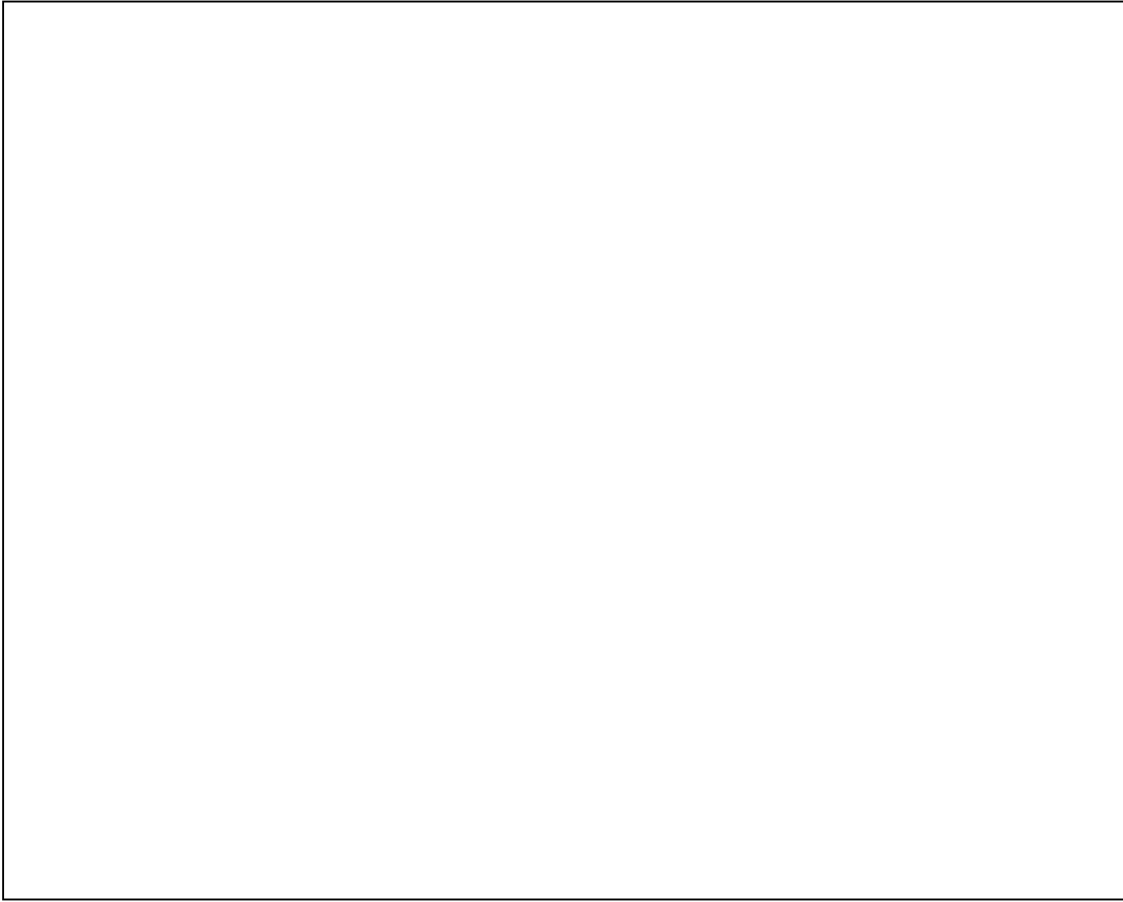
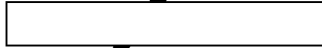
37. Active foreign involvement with the extreme left in Brazil appears to be minimal. What little evidence exists of Soviet and Cuban attitudes toward Brazil indicates, for example, that neither government believes there is much hope of stimulating significant popular agitation against the Brazilian regime any time soon. The Soviets almost certainly agree with the PCB's evaluation that their only chance for expanded influence is to tag along with the legal opposition, hoping that the change to a civilian-controlled political system will eventually work to its benefit. The Cubans provided some training in Cuba to MR-8 members in the 1970s and may have funded the training and travel to Nicaragua in 1979 of MR-8 activists who fought with the Sandinistas against the Somoza government. With the virtual demise of the MR-8 now, however, that opportunity no longer exists.

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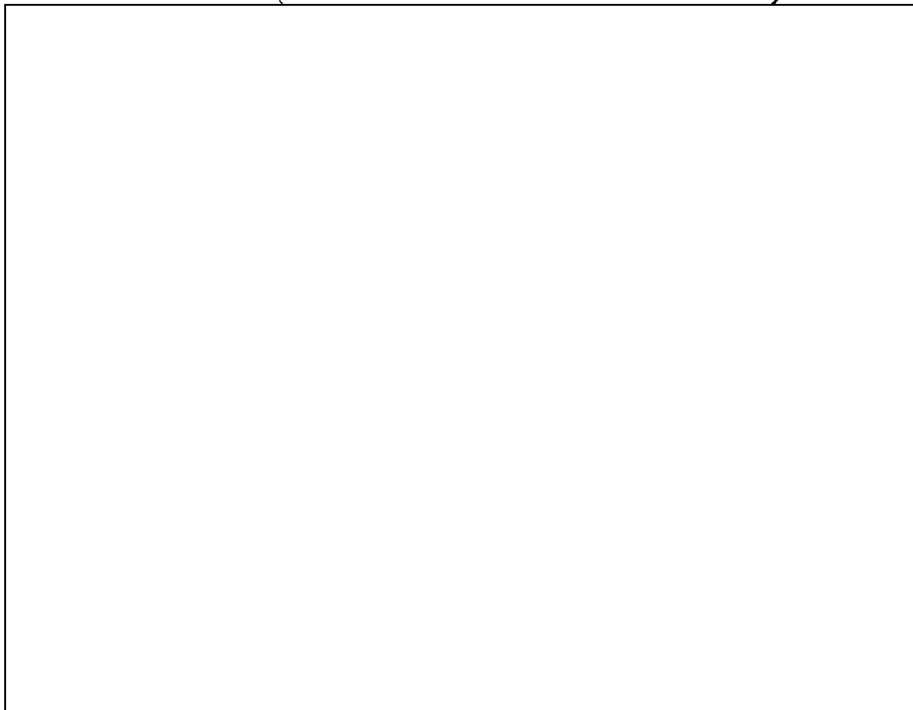
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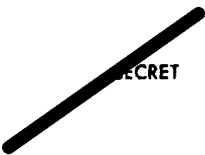
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