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Sub-Fonds: Records of President Robert S. McNamara

Fonds: Records of the Office of the President

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McNamara Papers

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Contacts with member countries: Brazil - Correspondence 01

BRAZIL

- 5/2/68 Dr. Helio Marcos Penna Beltrao, Minister of Planning and General Coordination
1. 5/22/68 General Alfonso Albuquerque Lima, Minister of the Interior
Ambassador de Cunha
2. 9/3/68 Antonio Delfim Netto, Finance Minister; Jose Maria Vilar de Queiros, adviser; Gen. Coun. Jayme Alipio de Barros; Charge Joage de Sa Almeida
10/2/68 Roberto Campos, former Minister of Planning
3. 10/22-10/26/68 Memoranda of Conversation during visit to Brazil:
10/23/68 (Rio) Mario Andreazza, Minister of Transport
Col. Ajace, Deputy Minister
Mr. Rezende, head of the Federal Highways Department
Col. Araujo, head of GEIPOT (Government agency supervising the Transport Survey)
- 10/23/68 (Rio) Jayme Magrassi Sa, President of BNDE
- 10/23/68 (Rio) Jose Costa Calvalcanti, Minister of Mines and Energy
Mario Bhering, head of Electrobras
John Cotrim, President of Furnas
- 10/23/68 (Rio) Dr. Octavio Rodriguez Lima, leading gynecologist; one time President of the Brazilian Society of Gynecologists *Filed in R. McHoffre*
- 10/24/68 (Recife) Euler Bentes, Head of SUDENE
- 10/24/68 (Bahia) Luiz Viana, Governor of the State of Bahia
Angelo Sa, Industrial Secretary of the State
Three other assistants
- 10/25/68 (Sao Paulo) Lelio Toledo Piza, President, State Bank of Sao Paulo
^{Gastao} Mr. Vidigal, President of the Banco Mercantil, Sao Paulo
Walter Lorch, President of a trucking firm, Sao Paulo
- 10/25/68 (Sao Paulo) Abreu Sodre, Governor, State of Sao Paulo
Luis Arrobas Martins, State Secretary of Finance
Herbert Levy, Secretary of Agriculture
Eduardo R. Yassuda, Secretary of Public Works
Firmino Rocha de Freitas, Secretary of Transport
Lelio Toledo Piza, President of the State Bank
Lucas Nogueira Garcez, President of CESP (largest power company in the State)
- 10/25/68 (Sao Paulo) Rubens vaz da Costa, President, BNB (Bank of the Northeast)
- 10/25/68 (Sao Paulo) Roberto Campos, former Minister of Planning

10/26/68 (Rio) Delfim Netto, Finance Minister
Ernane Galveas, President, Central Bank
Paulo Lyra, President of the Banco do Brasil
Vilar de Queiroz, principal assistant of the Minister
Several other officials in the Ministry of Finance

10/26/68 (Rio) Helio Beltrao, Minister of Planning
Mr. Velloso, Deputy Minister of Planning
Various other representatives

10/26/68 (Rio) Roberto Marinho, Editor of O Globo

10/26/68 (Rio) Augusto de Azevedo Antunes, industrialist (mining, banking and power interests)

10/26/68 (Rio) Candido Mendes de Almeida, lawyer and political scientist; visiting lecturer at Harvard, Columbia and other universities

10/26/68 (Rio) Mario Simonson, Vargas Foundation

10/26/68 (Rio) Luiz Ganzaga do Nascimento Silva, former Minister of Housing

Appointments without Memoranda of Conversation

10/22/68 (Rio) President Arthur da Costa e Silva

10/23/68 (Recife) Nilo de Souza Coelho, Governor of Pernambuco State

10/24/68 (Bahia) Luiz Viano Filho, Governor of Bahia State

10/23/68 (Rio) Luncheon hosted by Finance Minister Netto - list at end of Tab 3

10/24/68 (Rio) Cocktail party hosted by Gov., State of Bahia - list at end of Tab 3

10/23/68 (Sao Paulo) Julio Mesquita, Editor of Estado de Sao Paulo

10/26/68 (Rio) Nascimento Brito, Journal do Brasil

4. 12/12/68 Herbert Levy, Minister of Agriculture
Affonso Celso de Ouro-Preto, Second Secretary, Brazilian Embassy

5. 12/16/68 Robert Winters, President, Brazilian Light and Power Co.
Lars Bengston, General Counsel

3/6/69 Ambassador Mario Gibson Barbosa

*Filed
in
Small
office*

6. 4/9/69 Alexandre Beltrao, Executive Director, International Coffee Organization, and Executive Director, Coffee Diversification Fund
- 7/18/69 Almir Fernandes, Prof. of Architecture, Federal University of Parana; Head, Curitiba Metropolitan Area Planning Div., IPPUC, Curitiba
7. 2/16/70 Col. Jose Costa Cavalcanti, Minister of Interior
Rubens Vaz da Costa, President, Banco do Nordeste do Brazil
Ambassador Gurgel Valente
8. 5/25/70 Antonio Delfim Neto, Minister of Finance
Antonio Dias Leite, Minister of Mines and Energy
Mozart Gurgel Valente, Ambassador
Henrique Rodrigues Valle, Ambassador to the OAS
Paulo H. Pereira Lira, Director of the Central Bank
Jose Maria Villar de Queiroz, Advisor to the Minister of Finance
9. 9/23/70 (Copen.) Delfim Netto, Minister of Finance
Ernane Galveas, President, Central Bank of Brazil
Pereira Lira, Adviser
Eduardo da Silveira Gomes, Jr., Adviser
10. 1/5/71 Rondon Pacheco, Governor-elect, State of Minas Gerais
Camilo Penna, President, CEMIG
11. 2/8-9/71 Delfim Netto, Minister of Finance
Jose Maria Vilar de Queiroz, Economic Advisor to the Minister
Gustavo Silveira, Press Secretary to the Minister
12. 4/5/71 Delfim Netto, Minister of Finance
Jose Maria Vilar de Queiroz, Economic Advisor to the Minister
Mario Lopes Leao, President of COSIPA
Luis Fernando Sarcinelli, Executive Secretary, National Steel Council
Sergio C. de Weguelin Vieira, Economic Counselor, Embassy of Brazil
13. 5/3/71 Marcus Vinicius, Minister of Industry and Commerce
Gen. Alfredo Americo da Silva, President, CSN
Dr. Mario Lopes Leao, President, COSIPA
Dr. Luis Verano, Econ. Counselor, Embassy
14. 5/25/71 Dr. Joao Paulo dos Reis Velloso, Minister of Planning
15. 6/21/71 Delfim Netto, Minister of Finance
Ambassador Araujo Castro
Carlos Alberto Vieira, Rep. of Banco do Brazil in NYC
Ernane Galveas, President, Central Bank
15. 8/12/71 Ambassador of Brazil (Araujo Castro)
Thompson Flores, Embassy

17. 9/27/71 Antonio Delfim Netto, Minister of Finance
Dr. Ernane Galveas, President, Central Bank of Brazil
Jose M. Villar de Queiroz, Adviser to the Minister of Finance
Paulo H. Pereira Lira, Director, Central Bank of Brazil
18. 12/8/71 President Emilio Garrastazu Medici
19. 4/11/72 Antonio Delfim Netto, Minister of Finance
Ambassador Joao Augusto de Araujo Castro
Paulo H. Pereira Lira, Director, Central Bank
Jose Maria Vilar de Queiroz, Advisor on External Affairs,
Ministry of Finance
- 5/3-5/72 Fernando Henrique Cardoso, Director, Centro Brasileiro de Analise
(Bellagio) e Planejamento, Sao Paulo, Brazil
- 6/16/72 Vasco T. Leitao da Cunha, Rio de Janeiro
(NY)
- 7/24/72 Antonio Delfim Netto, Minister of Finance
(dinner at Villar de Queiroz, International Advisor to the Minister
home)
20. 3/26/73 Finance Minister Delfim Netto
Dr. Ernane Galveas, President, Central Bank of Brazil
21. 7/23/73 Dr. Alexander Beltrao, International Coffee Foundation
22. 8/1/73 Finance Minister Delfim Netto - Lunch with Mr. McNamara
- 6/15/74 Dinner hosted by Alexandre Kafka for:
Prof. Mario Henrique Simonsen, Minister of Finance
Paulo H. Pareira Loira, President, Central Bank of Brazil
23. 10/1/74 Finance Minister Mario Henrique Simonsen
President, Central Bank Paulo H. Pereira Lira
Director, Foreign Operations, Central Bank, Fernao Bracher
International Advisor, Finance Ministry Ary dos Santos Pinto
- 10/23/74 Dr. Roberto Campos
24. 2/7/75 Alexandre Beltrao, Executive Director, International Coffee Org.
25. 5/5/75 Joao Paulo dos Reis Velloso, Minister of Planning
- 6/12-13/75 Mario Henrique Simonsen, Minister of Finance
(Paris-Dev.
Cte.)
26. 6/30/75 Marcos Vianna, President of the National Development Bank
Zeuxis Neves, US Rep of Nat Dev Bank, and Attache at Embassy

27. 9/2/75 Mario Henrique Simonsen, Minister of Finance
Paulo H. Pereira Lira, President, central Bank of Brazil
Fernao Carlos Botelho Bracher, Director of External Area,
Central Bank
Ary dos Santos Pinto, International Advisor, Ministry of Finance
Alvaro da Costa Franco Filho, Head of the Division of
International Polices, Ministry of Foreign Affairs
Alexandra Kafka, ED, IMF
- 1/14/76 Felipe Herrera, Coordinator, ECIEL (Program of Joint Studies
on Latin American Economic Integration)
28. 3/1/76 Joao Paulo dos Reis Velloso, Minister-Chief of the Planning
Secretariat of the Presidency
Marcos Pereira Vianna, President, National Bank for
Economic Development (BNDE)
Zeuxis Neves, Attache of the Brazilian Embassy
29. 7/26/76 Joao Baptista Pinheiro, Ambassador to the U. S.
30. 10/2/76 Mario Henrique Simonsen, Minister of Finance
(Manila) Paulo Bellotti, Secretary-General, Ministry of Industry
and Commerce
Fernao Bracher, Director, Central Bank of Brazil
Ary dos Santos Pinto, International Finance Adviser,
Ministry of Finance
31. 10/14/76 Ambassador Joao Baptista Pinheiro
Zeuxis Ferreira Neves, Attaché
- 12/15/76 Sergio Correa da Costa, Ambassador to the UN
(New York) (At luncheon hosted by Amb. Akhund-Pakistan)
32. 2/11/77 Alexandre Beltrao, Chairman, International Coffee Organization
33. 2/22/77 Joao Paulo dos Reis Velloso, Minister in Charge of the
Planning Secretariat
Aderbal Costa, Head of the International Cooperation Section
in the Secretariat of Planning
Ambassador Joao Baptista Pinheiro
- 9/12/77 Eduardo Gentilo, Grandson of Ambassador Bunker
- 9/23/77 Finance Minister Henrique Simonsen, at dinner hosted by
Ambassador Penheiro
- 1/9/78 Paulo Jose Dutra de Castro - General Director of Industrial
Relations, Volkswagen, Brazil. [Education Panel lunch]
- 2/3/78 Dr. Walter Santos, Chairman, International Congress on
Food and Nutrition
34. 2/15/78 Paulo Villares, President of the Villares Group
Jose Guimaraes, Financial Vice President, Villares Group
35. 9/26/78 Mario Henrique Simonsen, Minister of Finance
Annual Meeting Paulo Lira, President, Central Bank
Fernao Bracher, Dir. of Central Bank
Luiz Barbosa, Central Bank
Alexandre Kafka, IMF ED; Ernesto Franco, IBRD ED

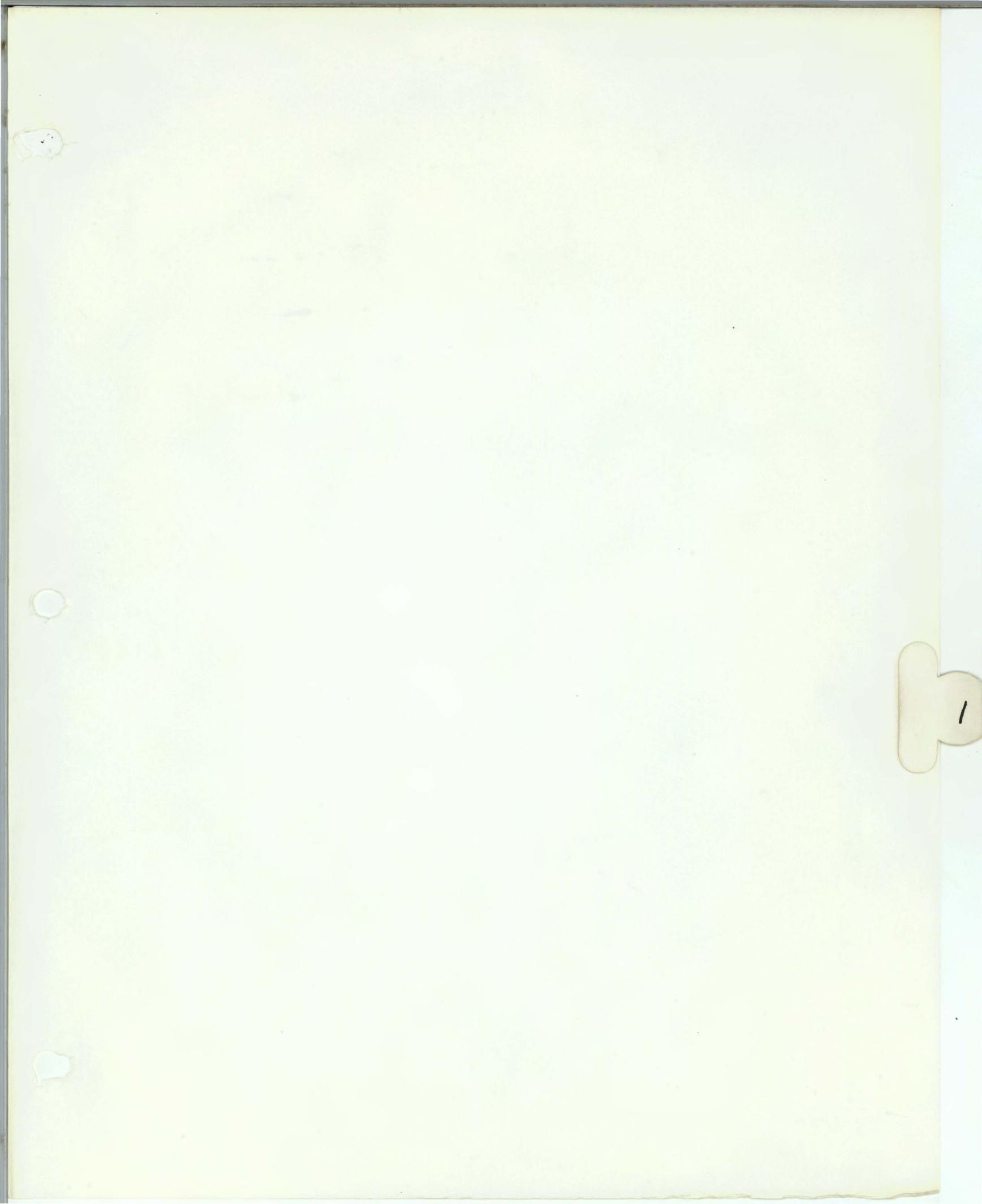
36. 1/5/79 Francelino Pereira, Governor-elect of Minas Gerais
37. 3/2/79 Jose Augusto Amaral de Souza, Governor-elect of Rio Grande
do Sul
Messrs. Kafka, Franco
38. 6/7/78⁹ Antonio Delfim Neto, Minister of Agriculture
Alexandre Kafka, ED-IMF
39. 6/19/79 Karlos Rischbieter, Finance Minister
Ambassador Silveira of Brazil
Alexandra Kafka, ED-IMF
40. 10/1/79 Karlos Rischbieter, Finance Minister
Annual Meeting (in Belgrade)
10/24/79 Ambassador Azeredo da Silveira
(lunch)
41. 11/6-13 RMcN Notes
1979
(Brazil)
42. 11/12/79 President Figueiredo
(Brazil) Minister of Finance Rischbieter

Met in Bahia:

Antonio Carlos Magalhaes, Governor of Bahia
Renan Balearo, Secretary of Agriculture, Bahia
Angelo Amaury Stabile, Minister of Agriculture
Ivan Araujo, Assistant to the Governor, Bahia
Amenair Grenalgh, POLONORDESTE Coordinator, Bahia

43. 2/19/80 Minister Antonio Delfim Neto, Chief of the Planning Secretariat
(In NYC) of the Presidency
Finance Minister Ernane Galveas
Sergio Faria Lemos da Fonseca, C/S to Delfim Neto
Jose Botafogo Goncalves, Head of Secretariat, Intl Econ & Tech Coord.
Gustavo Silveira, press assistant
Jose Carlos Maderia Serrano, Director of External Area, Central
Bank of Brazil
Alexandre Kafka, ED, IMF
44. 9/29/80 Ernane Galveas, Minister of Finance
Annual Carlos Langoni, President of Central Bank
Meeting Jose Flavio Pecora, Sec-Gen of Secretariat of Planning
Minister Jose Botafogo Goncalves, Sec of SUBIN
Carlos Serrano, Director of External Area of Central Bank
45. 12/3/80 Senator Lomonto
Amb. da Silveira
Mr. Barletta, OL
46. 12/10/80 Bishop Dom Haldar Camaro
1/27/81 Karlos Rischbieter, Finance Minister
(Lunch alone with Mr. McNamara)
47. 2/24/81 Ernani Galvaes, Minister of Finance
48. 4/27/81 Dr. Eliezer Batista da Silva, President of Companhia Vale do Rio Doce
Mr. Franca Pereira, Vice President " " " "
Mr. Samir Zraick, Financial Director, " " " "
49. 6/8/81 Mr. Alexander Beltrao, Executive Director, Internationals
Coffee Corporation
(No MemCon - Mr. McNamara saw alone)
- 6/12/81 Minister Antonio Delfim Netto, Minister of Planning
Mr Joao Camillo Penna, Minister of Industry & Commerce
(at lunch)

BRAZIL



OFFICE MEMORANDUM

TO: Files

DATE: May 23, 1968

FROM: Gerald Alter *GA*SUBJECT: Meeting of Mr. McNamara with Minister of Interior
of Brazil, General Afonso de Albuquerque Lima

Mr. McNamara met with the Brazilian Minister of Interior, General Albuquerque Lima, for approximately one half hour on May 22. Present at the meeting were the Brazilian Ambassador, Mr. Leitao da Cunha, Mr. Alexander Kafka, Brazilian Executive Director in the International Monetary Fund, several associates of the Minister, a State Department guide and an interpreter. Messrs. Knapp and Alter were also present.

The Minister repeated an invitation to Mr. McNamara from the Government to visit Brazil at the earliest opportunity. Mr. McNamara indicated that he greatly appreciated this invitation and would accept it as soon as possible.

The Minister indicated that the Brazilian Government would very much like to present to the Bank two series of projects for financing. The first was a series of sanitation projects in several Brazilian cities. The second was a group of irrigation projects in Northeast Brazil. Most of the meeting was devoted to an exchange of views between Mr. McNamara and the Minister on the second group of projects. The Minister explained that the Northeast is a critical area for development and that two weeks ago the President of Brazil made a very important statement on the irrigation program in the Northeast. Irrigation would expand basic food crops as well as develop lands for cattle. Industry is developing much more rapidly than agriculture in the Northeast and the Government feels that it is important to establish a better balance between agriculture and industry by accelerating agriculture. Mr. McNamara stated that the Bank wants to complement efforts that Brazil itself is making to shift funds from the rich areas of Brazil to the poor areas such as the Northeast. Moreover, he concurred with the emphasis which the Brazilian Government appears to be giving to agricultural development but he indicated that the Bank would have to be satisfied that the return on capital invested in particular irrigation projects was satisfactory. The Minister assured him that all projects now being formulated in the Northeast are being considered from the standpoint of economic feasibility.

The Minister also raised the question of IDA assistance for Brazil, requesting the Bank to consider such assistance for the agricultural projects in the Northeast even if Brazil does not qualify for IDA assistance under the present per capita income limit of US\$250.- (Comment: The Minister was misinformed on the Bank's evaluation of Brazil - we

consider Brazil to be eligible for IDA assistance according to the poverty test but not according to the creditworthiness test.) Mr. McNamara indicated that we are perfectly prepared to consider Bank loans for high-yielding agricultural projects in the Northeast but that we have no IDA resources at present and it is impossible to say when these resources will be replenished.

The meeting closed with the Minister stating that he will arrange for the presentation of the two groups of projects to the Bank. Mr. McNamara expressed his feeling that there should be great opportunities for the Bank to assist Brazil, but that much needed to be done both by the Bank and Brazil if external assistance to Brazil were to make its proper contribution. He knew that there were internal policy problems in Brazil that needed to be resolved and we were prepared to help with our advice and in any other appropriate manner.

Cleared with and cc.: Mr. Knapp
cc. Messrs. McNamara
Chadenet
Evans
Armstrong
Wiese

GAlder:pb

OFFICE MEMORANDUM

TO: Mr. McNamara (through Mr. Knapp)

DATE: May 16, 1968

FROM: Gerald Alter *gh.*SUBJECT: BRAZIL: Background for your meeting with Minister of the Interior,
General Albuquerque Lima, on May 22

1. A biographical summary on the Minister is attached. He is said to belong to the nationalistic wing of the armed forces and to favor strong military rule in Brazil for many years to come. His influence on economic development rests mainly on two foundations: (1) he supervises the National Housing Bank (which receives substantial tax resources); (2) he also supervised SUDENE, a federal agency for the development of the Northeast of Brazil, which equally is the recipient of substantial federal funds. Bank staff has not yet had substantive contacts with him. Members of other agencies have informally conveyed to us their impression that the Minister is "not used to thinking in terms of economic opportunity costs." ✓
2. The Minister is likely to raise the question of Bank lending for housing, sanitation and projects in the Northeast. The first has been outside the scope of our lending possibilities. Nevertheless, given the importance of the sector for the absorption of federal resources, a 1967 economic mission has analyzed the sector and prepared an Annex on housing development in Brazil.
3. As regards sanitation, we are planning to send a mission in September to help identify sanitation projects in a number of small Brazilian cities. It is possible that some of the selected cities may be in the Northeast. ✓
4. In the Northeast, our activities in recent years have consisted only of project preparation. Generally, project preparation in the Northeast has been slow and of poor quality, while both the IDB and the AID have been eager to pursue any project lead that developed. The IDB, in particular, has been eager to find projects in the area to which to attach Social Progress Trust Funds. Probably for this reason the Government has not yet approached us in respect of a project in that area. ✓
5. The first phase of the Bank-directed Transport Survey has identified a port project in Recife on which preliminary engineering is being done. As soon as we have completed negotiations with the Government on a Memorandum of Understanding on their future transport policies (on which we have briefed you recently), we are planning to send a pre-appraisal mission covering three ports, including Recife. ✓

President has seen

Moreover, the present second phase of the Transport Survey covers the road network of the entire Northeast and is expected to identify early next year numerous high priority road projects in that area for which Bank lending would be considered. ✓

6. In agriculture, we are awaiting the initiation of operations under our recent livestock loan to follow up with a project identification mission for additional agricultural credit. The mission would, inter alia, look into the possibilities of extending our lending for livestock into the Northeast and of initiating other credit programs in that area such as sugar diversification. Agricultural infrastructure projects, e.g., irrigation and land settlement, are presently proceeding in the Northeast with the assistance of the IDB and AID. The Bank so far has not been approached to consider such projects, but the Minister may do so during his meeting with you. So far we have not actively explored such project possibilities because the few projects investigated to date have made us suspect that many of them might have comparatively low rates of return. ✓ ✓ ✓

7. Informal discussions were held two years ago between Bank staff and key executives in the electric energy sector about the possibility of Bank financing for rural electrification in the Northeast. Discussions ended when the AID and IDB absorbed the project and it became apparent that its foreign exchange content would be low.

Recommendation

8. You may wish to inform the Minister about our project preparation efforts for the expansion of the port of Recife, roads in various states in the Northeast, and agricultural credit and sanitation projects including the Northeast area. You may also wish to point out to him that if the replenishment of IDA resources were to be forthcoming on a level substantially above that of the past, we would consider contributing some IDA resources to some of the projects we might finance in the Northeast. ✓ ✓ ✓

Att.

cc: Messrs. Knapp
Alter
Baum
Evans
Armstrong

Biographical Data on Minister of the Interior
Afonso Augusto de Albuquerque Lima

Minister of the Interior since the beginning of
regime of President Costa e Silva (March 1967)

Date of Birth: August 22, 1909

Military Life:

Entered military service	April 1, 1927
Cadet	June 21, 1930
2nd Lieutenant	July 24, 1930
1st Lieutenant	Aug. 13, 1931
Captain	Oct. 2, 1934
Major	Dec. 25, 1942
Lt. Colonel	Sept. 25, 1947
Colonel	June 25, 1953
Brig. General	July 25, 1964
Major General	March 25, 1966

During World War II, he participated in the Brazilian Expeditionary Forces as a member of the Ninth Battalion of Engineers. During his military career he has also taught at the Superior War College, commanded roadway construction, and commanded the Second Cavalry Division. He was Director-President of the National Department for Works against drought.

OFFICE MEMORANDUM

9/30-
5/22

TO: Mr. Robert S. McNamara

DATE: May 10, 1968

FROM: J. Burke Knapp

SUBJECT: Appointment for *J. Kafka* Brazilian Minister of Interior

Alexandre Kafka, the Brazilian Director in the Monetary Fund, telephoned me this morning to ask for an appointment with you week after next with the Brazilian Minister of Interior, General Alfonso Albuquerque Lima. He said that General Albuquerque Lima represents the nationalist element in the Cabinet, in contrast to Mr. Beltrao (whom you saw recently) on the liberal wing, and he thought it important that you "play both sides."

Apparently General Albuquerque Lima has important responsibilities for the coordination of development plans in the undeveloped parts of Brazil (e.g. the Northeast) and it is a sore point with him that we have not allocated IDA funds to Brazil. Kafka said that he had in fact advocated Brazil's withdrawal from IDA on these grounds.

cc: Mr. Alter

*Alter + Kafka
advised by Knapp*

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT
ASSOCIATION

INTERNATIONAL FINANCE
CORPORATION

OFFICE OF THE PRESIDENT

May 10

11:50 Mr. Kafka - Mr. Albuquerque Lima will be in Washington from May 19 to 22nd (he leaves at 4 p.m. on the 22nd). Monday and Tuesday have been reserved for American Agencies, Wednesday, May 22nd for International agencies. Mr. Kafka suggests that Mr. Albuquerque Lima could see Mr. McNamara early on Wednesday. (Mr. Kafka has a Board Meeting starting at 10:00 a.m.)

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: September 3, 1968

FROM: Gerald Alter *GA*SUBJECT: Meeting of Mr. McNamara with Minister of Finance of Brazil,
Mr. Antonio Delfim Neto

The Brazilian Minister of Finance, Mr. Delfim Neto called upon Mr. McNamara accompanied by his advisor, Mr. Jose Maria Vilar de Queiros; General Counselor, Mr. Jayme Alipio de Barros; Chargé d'Affairs, Mr. Joage de Sa Almeida and Messrs. Kafka and Gomes, Brazilian Director and Alternate in the IMF. Messrs. Knapp and Alter were also present. The Minister confirmed the invitation to Mr. McNamara to visit Brazil in October and Mr. McNamara indicated that he should be able to spend four days in Brazil. He expressed particular interest in visiting the Northeast. It was agreed that the staff would work out the details for his trip. The Brazilian Government offered to provide aircraft for travel within Brazil.

Mr. McNamara said that the Bank was very much interested in expanding the scale of its operations in Brazil if Brazilian performance, both overall and in the particular sector where the Bank would be lending, was adequate. Our recent rate of lending had been averaging US\$60 million and he would like to see it triple or quadruple in the next couple of years in response to improving Brazilian performance. The current Bank loan for highways was an example of Bank response to Brazilian performance. He understood that the transport letter which was being delivered to the Bank today went a long way in clarifying Brazilian policy in the transport field and that on this basis we were prepared to proceed with the highway loan. On the other hand, there were two matters on which the letter was silent and on which we were not completely satisfied: 1) reforms in the organization and management of the railways and 2) a study to identify additional uneconomic railway lines which should be closed. We would want Brazilian authorities to give consideration to these two matters as we move ahead in preparing additional loans for the transport sector. The Minister did not respond.

There was some discussion on fields in which Bank lending might expand including education and industry. The Minister expressed definite interest in obtaining Bank assistance for education and confirmed that the Bank could contribute to industrialization in Brazil by operating through credit intermediaries. The Minister also seemed to welcome the Bank's increased interest in Northeast Brazil.

The Minister mentioned that the manufacturing sector now seemed to be expanding at a faster rate and he would expect a 7 to 9 percent rate of growth for the next couple of years. He also observed that GNP is expanding this year at a more substantial rate even though coffee has not increased and adverse weather was affecting crops in particular regions. The recent devaluation, coming as it does at the time before the planting season, should help encourage cash crops, particularly for export.

President has seen

The Minister indicated Brazil's interest in obtaining IDA assistance. Mr. McNamara responded by saying that there was some possibility, but that this depended on IDA replenishment, prospects for which were not very encouraging at the moment.

The question of a possible Consultative Group for Brazil was raised. The Brazilians indicated that they saw many advantages in carrying out separate discussions with each of the lending agencies.

It was agreed that Mr. Alter and his colleagues would, during their visit to Brazil around September 11, discuss in greater detail the composition of a Bank lending program and related performance conditions. This could be followed up by further discussion when the Minister visits Washington during the annual meeting as well as during Mr. McNamara's visit to Brazil in October.



3

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: November 20, 1968

FROM: Gunter K. Wiese *hw*~~Confidential~~SUBJECT: BRAZIL: Meeting of Mr. McNamara with
Minister of Transport, MARIO ANDREAZZA

On October 23, Mr. McNamara called on Mr. Andreazza. Also present were Col. Ajace, Deputy Minister (part of the time); Mr. Rezende, head of the Federal Highways Department; Col. Araujo, head of GEIPOT (the Government agency supervising the Transport Survey) and Messrs. Alter and Wiese.

Mr. McNamara inquired about the prospects for reducing the railway deficit. The Minister stated that the Government was implementing all of the consultant's recommendations contained in the recently completed Transport Survey and noted that already much progress had been made. He was confident that further progress is in prospect, but appealed to the Bank for assistance. An internationally reputed firm of consultants would soon be engaged to assist in the implementation of the Survey's recommendations. In reply to a question by Mr. McNamara about the likely size of the 1968 railway deficit, the Minister handed him a table showing some reduction as compared with 1967, but it was impossible to identify the dollar amount from the table because the cruzeiro figure shown was obviously in terms of values several years back and no conversion rate into dollars was indicated. After some discussion, a figure of about \$200 million was given as the estimate for 1968. The Minister also undertook to provide the Bank by the end of November with an estimate for the deficit in 1969, but he did not elaborate on this further. He did, however, state that this estimate would reflect the action the Government is planning to take in terms of railway reforms and improvements.

Concerning the investment program of the railways, the Minister said that about \$60 million a year is expected to be expended on new railway investments until 1973. In this context, Mr. McNamara referred to the prospective investments by Central do Brasil in conjunction with the Hanna/Antunes iron ore export project. The Minister stated that he had the needs of that project very much in mind.

Turning to highways, Mr. McNamara inquired about the investment program and the breakdown between federal and state construction activities. Mr. Rezende explained that in 1968 total highway investment expenditures (in addition to maintenance) were running at about \$400 million, divided about equally between federal and state expenditures. Highway investment in Brazil was presently growing at about 15 percent per year. All investments proceeded in accordance

*File in the
minutes of
conversation
book*

with the Master Plan prepared by the Transport Survey. Agreements between the Federal Government and the states concerning the reorganization of the Highway Department were in the process of being signed. The division of responsibility between the Federal Government and the states in respect of highway investments was based on which of the entities owned the roads. This was an admittedly empirical division reflecting past haphazard decisions concerning the allocation of roads to the states and the Federation. New legislation was being prepared to divide the road network in the future according to the Master Plan. All inter-state roads would be federal. The entire secondary system would go to the states. Responsibility for regional roads would be divided road-by-road between the states and the Federal Government.

Mr. McNamara inquired how the annual highway investment expenses would in the future be broken down among the three compartments described above. Mr. Rezende replied that this would depend on an assessment of the priority standing of each road. Legislation regulating the allocation of roads was being prepared and the Government would deliver on its commitments to the IBRD to have such legislation enacted by the end of 1969. Since all road construction was being financed by the Federal Highway Fund, the resources for which were being collected by federal agencies, the Federal Government would, in any event, exercise considerable control over road construction priorities. The new legislation would, however, give explicit recognition to the federal prerogative of determining priorities.

In reply to a question by Mr. McNamara, Mr. Rezende stated that no more than roughly 10 percent of the current investment expenditures on highways in all of Brazil is for "political" roads.

An attempt on the part of Mr. McNamara to initiate a discussion of the current problems and prospects for Brazilian ports was not successful largely because of the absence of a representative of the Federal Port Administration.

cc: Mr. McNamara (through Mr. Steckhan)
Mr. Sadove
Mr. Paterson
Mr. Husain

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: November 20, 1968

FROM: Gunter K. Wiese *hw*ConfidentialSUBJECT: BRAZIL: Meeting of Mr. McNamara with
Finance Minister, DELFIM NETO

On October 26, Mr. McNamara accompanied by Messrs. Alter and Wiese called on Minister Delfim Neto. The meeting was attended by the President of the Central Bank, Mr. Galveas; the Director of the Central Bank responsible for external finance, Mr. Paulo Lyra; the President of the Banco do Brasil, Mr. Hector Jost (part of time); and the principal assistant of the Minister, Mr. Vilar de Queiroz, as well as several other officials in the Ministry of Finance.

The Minister summarized briefly current economic trends in Brazil. During 1968, GNP is likely to increase by 6-7 percent, as compared with the target of 6 percent. The rate of increase in the Northeast will be 8 percent. Prices at the end of the current year will probably be 25 percent higher than a year earlier. This had been expected. The projected reduction in the fiscal deficit is likely to be achieved, largely because of an increase in revenues. The latter is due primarily to a doubling in the collection of the consumption tax. The rate of this tax was recently raised by 30 percent and this, together with rising prices, has produced substantial additional revenues. Current expenditures remain a difficult problem for the Government. Much depends on the success of the Government in reducing the number of federal employees (presently totalling roughly one million). A new law establishes ceilings on federal employees by sectors of activity. Another favorable development is the prospective reduction in 1969 in the fiscal deficits of the States, which is likely to result from ceilings established by the Federal Government on State borrowing.

Between June and August of this year, the monetary situation has improved significantly. The Minister expects the rate of expansion in the money supply to decline to an annual level of 27 percent in November as compared with 30 percent in September.

According to the Minister, foreign exchange reserves have risen only \$8 million since the beginning of the year. The targeted \$25 million increase during 1968 is thus unlikely to be reached. The Government remains determined to pursue a flexible exchange rate policy. He expects 1968 exports to total \$1.8 billion, which would represent a 10 percent increase over 1967. Commodities mainly accounting for the increase are meat, corn and rice. The flexible exchange rate policy has gone a long way toward restoring the confidence of exporters. An additional factor stimulating exports has been a relatively easy credit policy for agricultural loans.

The Minister stated that his major concern on the economic policy front is the prospect for sizeable wage increases. After the tight policy pursued during 1966 and 1967, the Government will probably have to be more generous from now on. Labor courts are now granting 30 percent annual increases instead of the 24 percent recommended by the Government. The Government is trying to persuade the labor courts to exercise moderation.

Industrial employment is good and the production figures reflect this. Between December 1967 and September 1968, automobile production rose 20 percent, cement 11 percent and steel 14 percent. The 1969 harvest promises to be poor in the Northeast, but he expects it to be good in the remainder of the country.

The Minister said that the Government will continue to follow its present coffee policy aimed at maintaining constant the real revenues of the producers. During the current year, only 18 million bags were purchased under the coffee support scheme as compared with 26 million bags during the preceding year. There are now 61 million bags in stock, of which 22 million are probably no longer saleable; the remaining 39 million bags represent a two-year supply.

Mr. McNamara referred to the need for large capital investments in industry and agriculture and inquired about the Government's intentions regarding the present practice of Government banks to lend at negative real interest rates. The Minister replied that he agreed with the Bank in principle on the harmful effects of this practice in terms of resource allocation. There is, however, a practical question as to when and in what form full monetary correction could be introduced into the lending practice of these banks. Such correction could be effected by charging interest rates which in nominal terms exceed the rate of inflation. It could also be achieved by a variety of indexing schemes. As regards the latter, it is difficult to find the right index for all types of loans. Mr. Alter referred to the indexing arrangements made under the recent IBRD loan for livestock as an example which might guide the Government in working out a proper indexing system. The Minister commented that proper indexing could probably be devised for loans financing equipment, but indexing might be difficult on loans for working capital. All such loans in Brazil are, however, already being made at positive interest rates. He then expressed concern about the negative effect on inflationary expectations of any widespread application of indexing to agricultural and industrial lending. In conclusion, the Minister suggested that the Bank, at least for the time being, leave the problem of negative interest rates in his hands. He would try to move to a solution as soon as possible.

Mr. McNamara questioned the Minister on the Government's reaction to the Bank's five-year lending program which the September 1968 mission had discussed with him. Mr. Delfim Neto expressed agreement in general. He suggested, however, that the Bank consider expanding substantially its allocation for irrigation. Mr. McNamara concurred in principle, but added

that some of the projects that had come to the Bank's attention prima facie seemed to have a low rate of return. In order to enable the Bank to consider financing these projects, they would have to have satisfactory rates of return. Mr. Delfim Neto suggested that in computing the rate of return, sufficient allowance should be made for the benefits accruing from any stabilizing effects on food prices and the cost of living. Such effects, of course, could only be achieved if additional storage capacity were also provided. There was consensus that the cropping pattern of the irrigation projects would have to be based on staple foods. Mr. Alter noted that the projects he had seen in the Northeast seemed to have a high percentage of the area allocated to forage crops. Mr. McNamara said that the Government and the Bank may have to work together to modify the projects so as to improve their return.

During the ensuing discussion, the Minister agreed with Mr. McNamara that the major claims on resources competing with the irrigation projects are the proposed investment for infrastructure in the Central and Southern States. The Minister stated that he personally placed low priority on local infrastructure projects such as those for sanitation. As regards projects in the State of Sao Paulo for which Bank assistance has been requested, he deemed the Capivara hydro project to be well justified. He would also welcome Bank financing for the Sao Paulo beltway. Mr. Alter emphasized that any consideration by the Bank of projects in Sao Paulo other than those already in our current lending program should be preceded by a review of the overall budget picture in the State and the metropolitan area. This would permit a judgment as to whether adequate efforts to raise internal resources are being made in relation to the legitimate needs. The Minister expressed the view that both the 17 percent State turnover tax and the municipal property tax (which together account for the bulk of revenues in the Sao Paulo area) are already high and should not be increased in order to avoid even larger tax evasion than is already being practiced, particularly in the agricultural sector. He agreed with Mr. Alter that the efforts of the State should rather go in the direction of exercising restraint on investments. He conceded that the projects outside the federal plan, of which there are several in the State of Sao Paulo, have not as yet been put through a careful priority screening.

The Minister then explained that the restrictions on IBRD loans relating to the financing of cruzeiro expenditures as well as the limitation to 15 percent of the margin of protection granted to Brazilian suppliers (participating in international competitive bidding under IBRD loans) were causing the Government difficulties in the execution of its development program. He felt that the best solution for these problems would probably be an IBRD program loan to Brazil.

Mr. Lyra explained that the Government is presently developing for the first time a clear policy on its external debt. Projections until 1980 of this debt are being prepared and will be subject to a computer study which he expected to be completed in 2-3 months. He undertook to send the study to the Bank and was assured by Mr. McNamara that we would carefully review it and take it into account in formulating the terms of our future lending to Brazil.

cc: Mr. McNamara (through Mr. Steckhan)
Mr. Knapp
Mr. Friedman
Mr. Evans
Mr. Knox
Mr. Diamond
Mr. Husain
Mr. Weiner/Mr. Lerdau

GKWiese:bjp

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: November 20, 1968

FROM: Gunter K. Wiese

~~Confidential~~SUBJECT: BRAZIL: Meeting of Mr. McNamara with
Minister of Mines and Energy, JOSE COSTA CAVALCANTI

On October 23, Mr. McNamara called on Minister Cavalcanti. Also present were Mr. Mario Bhering, head of Eletrobras; Mr. John Cotrim, President of Furnas; and Messrs. Alter and Wiese.

The Minister handed Mr. McNamara a brief memorandum summarizing the present condition and prospects of Brazil's electric energy sector. The paper emphasized that Brazil's power capacity consumption of electric energy is presently 350 KWH per year, which level was reached in the United States in 1915. Consumption is growing at about 11 percent per year, with the Northeast reaching 13 percent. In 1980, per capita consumption is expected to reach 1,000 KWH. The memorandum describes present and future capacity levels and the investment program needed to achieve the projected growth. The current investment program runs at about \$600 million annually and almost 80 percent of this is being financed internally. Next year about \$150 million of external financing will be required.

The ensuing discussion largely took the form of reviewing the memorandum. Mr. Bhering stated that the projection of per capita consumption until 1980 is based on a mere extrapolation of current trends. He agreed with Mr. McNamara that per capita consumption in 1980 was probably understated in the memorandum.

The Minister and his associates pointed out that they were looking to the official lending agencies for covering most of the financing gap in their investment program. Even though they recognized that the electric energy sector was ideally suited for attaching bilateral finance to the investment program and could thus help Brazil to achieve her overall capital inflow targets, they felt that Brazil would have to pay a high price for this. Taking into account the interest rate differential between official lenders and bilateral finance; the difference in amortization periods between, say, 25 and 15 years; and - most importantly - the lower cost and greater range of equipment obtainable under international competitive bidding, a World Bank-financed project could probably acquire its equipment at a cost roughly one-third lower than that of equipment imported under suppliers credits.

Mr. McNamara emphasized that there was essentially no limit on the volume of IBRD lending to Brazil, provided three conditions were met: (1) that the projects were sound; (2) that the environment was sound; and (3) that the country had the ability to repay the loans. He added that

our present allocation of \$50 million per year in the five-year lending program for Brazil's electric energy sector is flexible. Any increase would depend, apart from the above three conditions, on the progress made with preparing bankable projects in other sectors in Brazil.

There followed a brief discussion on the pending initiation of a nuclear energy program in Brazil. Mr. Bhering explained that in about 15 years Brazil would, at least in many parts of the country, run out of high-quality hydro sites. Some of the large sites left in the south might not be useable because they are on international rivers. In any event, some thermal power would be needed to firm up the hydro system, and the point had been reached where in the next few years a pilot nuclear station should be constructed. Mr. Cotrim explained that the Government would hope to explore with the Bank the possibility of attaching to such pilot project a Bank loan for its conventional equipment. It seemed unquestionable that the reactor itself would have to be purchased bilaterally. X

Although the Minister's responsibilities also include the mining sector, a shortage of time and the apparent lack of familiarity of the Minister with the investment requirements and problems of the sector resulted in only a brief and rather general discussion of the sector.

cc: Mr. McNamara (through Mr. Steckhan)
Mr. Knox/Mr. King
Mr. Husain

GKWiese:mr

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: November 19, 1968

FROM: Gunter K. Wiese *GW*~~Confidential~~SUBJECT: BRAZIL: Meeting of Mr. McNamara with
Governor of State of Sao Paulo, ABREU SODRE

On October 25, Mr. McNamara, accompanied by Messrs. Alter and Wiese, called on Governor Abreu Sodre. Also present were: Luis Arrobas Martins, State Secretary of Finance; Herbert Levy, Secretary of Agriculture; Eduardo R. Yassuda, Secretary of Public Works; Firmino Rocha de Freitas, Secretary of Transport; Lelio Toledo Piza, President of the State Bank; and Lucas Nogueira Garcez, President of CESP (the largest power company in the State, which is also a Bank borrower).

The Governor initiated the discussion by presenting some salient facts on the economy of the State which he called the dynamo of Brazil. The level of unemployment in the State at present is low. Its average per capita income is about \$500. It produces 52 percent of all federal revenue and 57 percent of the 34/18 funds flowing into the Northeast. Its urban population amounted to 53 percent in 1950, 62 percent in 1960, and now accounts for 70 percent of the State's population. Although the State has a low birth rate, the progressive urbanization of the State materialized because of migration from other States. Over the last 13 years, the birth rate in the State had declined from 35.6 per thousand to 27.7 per thousand. Nevertheless, the infrastructural capacity is falling rapidly behind. The Governor said that the metropolitan area of Sao Paulo is growing at an annual rate of 6 percent.

The Governor then requested IBRD assistance for the following sectors:

1) Water Supply and Sewerage in the Sao Paulo Metropolitan Area

The present population of Sao Paulo of about 7 million people is expected to triple by 1990. Only 60 percent of the area is presently served by the water system and only 35 percent is connected with sewerage facilities. He deemed it ironic that by 1970 roughly 70 percent of the urban areas in the Northeast may be connected while Sao Paulo, unless something drastic is done, would certainly show a much lower percentage. Investment in sanitation should certainly have top priority.

2) Education

The Governor considered this a second priority for the State investment program. At present, the State is spending 28 percent of its

revenues on education - as much as the country as a whole. He is planning to raise this percentage to 30 percent next year.

3) Agricultural Projects

He did not elaborate on this.

4) Electric Energy

Power consumption in the State is growing at a rate of over 10 percent per annum. He then had Mr. Lucas Garcez hand over an official application for Bank loans for three power projects to be carried out by CESP, i.e.,^{1/}

- (a) Capivara (requiring an external loan of about \$60 million).
- (b) Promissao (an external loan of perhaps \$30 million may be required).
- (c) Agua Vermelha (which would probably need an external loan of about \$100 million).

5) The Sao Paulo Beltway (no further comments were made)

6) The Sao Paulo Railway (no further comments were made)

7) The new Santos Freeway (no further comments were made)

The Governor emphasized that despite its relatively high per capita income, the State of Sao Paulo is still in dire need of external capital. The State provides 52 percent of the federal revenue but receives back only 1.2 percent. Only a small fraction of federal expenditures goes to the State. In reply to a question by Mr. McNamara, he said that he expected present tax rates in the State to continue. This is essentially a question of the tax rate of the turnover tax - now at 17 percent - which produces 96 percent of the Sao Paulo State revenue. He considered this level already too high to render any additional increase feasible and in this context alluded to widespread tax evasion in the State.

Mr. McNamara indicated that he was fully convinced that the need for more infrastructure in the State is indeed sizeable, but that it appeared still more manageable than the need in the Northeast of Brazil. Mr. Alter added that the recent constitutional reform had resulted in an increasing flow of resources to the states and municipalities at the expense of the Federal Government. What was needed from the point of view of Brazil as a whole was to shift more investment functions and responsibilities back to the States. The Secretary

^{1/} A reply is being prepared in the Bank.

of Finance pointed out that the total expenditures of the State were already at a level of NCr 4 billion a year. He conceded that an increase in the 17 percent turnover tax by, say, 2 percentage points, would raise over NCr 400 million of additional revenue, which would go a long way toward solving some of the infrastructure investment problems in the State. He reiterated, however, that the 17 percent sales tax rate had to be considered a maximum feasible under present circumstances.

cc: Mr. McNamara (through Mr. Steckhan)
Mr. Sadove
Mr. Knox
Mr. Ballantine
Mr. Husain

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: November 18, 1968

FROM: Gunter K. Wiese *GW*SUBJECT: BRAZIL: Meeting of Mr. McNamara with
Minister of Planning, HELIO BELTRAO

On October 26, Mr. McNamara accompanied by Messrs. Alter and Wiese called on Minister Beltrao. There was first a short private meeting during which Mr. Velloso, Deputy Minister of Planning, was also present. It was followed by a larger meeting in which numerous representatives of other Ministries and government agencies also participated.

The discussion was initiated by a question from Mr. McNamara on the priorities in Brazil's capital investment budget. He deemed this a key question, given the fact that investment requirements in Brazil substantially exceed resources. The Minister explained that Brazil was now embarking on a three-year investment plan which reflected a new investment strategy and was based on the assumption that it would be supported by the IBRD. He had reviewed the Bank's five-year lending program and deemed it generally acceptable, provided some flexibility would be maintained in the later years. He said the Government would welcome it if the Bank could make larger allocations for irrigation and sanitation. Mr. McNamara replied that the Bank would be glad to expand its projected lending in these fields provided this is economically justifiable.

There was consensus that the expansion of the electric energy sector was proceeding in a well-coordinated fashion. As regards the investment program of the State of Sao Paulo, Mr. McNamara inquired about the Federal Government's view on the investment priorities in the State, which is confronted by a tremendous need to expand its infrastructure. Mr. Velloso stated that the Government generally endorsed the program of the State but indicated that the Sao Paulo subway so far is not yet included in the overall federal investment program.

The Minister emphasized that the Government will make efforts to sell the three-year plan to the politicians and the public. Arrangements are already being implemented to improve the administrative machinery necessary for executing the plan. So far the plan has only the status of an executive plan and Congress still has to approve individual pluriannual investment budgets. The Minister hopes that this can soon be changed so that Parliamentary action relevant to the plan's execution would take place only once at the beginning of the plan period.

There followed a systematic presentation of the major content of the three-year plan. Briefly, the plan provides for public investment expenditures by the Federal Government over the next three years of NCr 32 billion in current prices. Another NCr 7 billion is envisaged to be spent by the states and municipalities for projects not included in the federal plan.

The breakdown of the above NCr 32 billion figure is as follows:

	<u>NCr Billion</u>
Electric energy	6.0
Housing	5.0
Transport	5.2
Petroleum	2.3
Communications	1.1
Education	8.0
Industry	4.4

of which:

Steel	1.1
Mechanical	1.1
Chemical	1.1
Mining	0.6
Non-ferrous	0.5

32.0

cc: Mr. McNamara (through Mr. Steckhan)
Mr. Knapp
Mr. Evans
Mr. Knox
Mr. Husain
Mr. Lerdau

OFFICE MEMORANDUM

TO: Memorandum for Record

FROM: Gunter K. Wiese

SUBJECT: BRAZIL: Meeting of Mr. McNamara with
Head of SUDENE, EULER BENTES

DATE: November 18, 1968

~~Confidential~~

On October 24, Mr. McNamara, accompanied by Messrs. Alter, Clark, Steckhan and Wiese, called on Mr. Euler Bentes. Also present were Col. Stanley, deputy head of SUDENE; his substitute, Mr. Deniz Xavier; and Mr. Rubens Vaz da Costa, President of the Banco do Nordeste.

The first part of the meeting took place in the presence of a large audience. Mr. Euler Bentes made a summary presentation of the economic problems in the Northeast and of SUDENE's past and present activities. The Bank representatives were handed summary tables of the data referred to.^{1/}

The second part of the meeting was held in a smaller conference room, with only the senior staff of SUDENE being present.

Mr. Euler Bentes pointed out that the population of the Northeast presently totals 27 million, or 31 percent of Brazil's total population. Public per capita investment in the Northeast is about \$300 per year. Over the last eight years, growth in agricultural output has been 6 percent, and in industrial output 9 percent. Agriculture now accounts for about 46 percent of regional GDP, and industry for about 13 percent. SUDENE operates within the framework of indicative development plans. A new plan covering the next three years has just been approved by the Federal Legislature. The plan covers only the public sector. It is estimated that the activities of the plan would absorb from 10-15 percent of the GDP in the Northeast. A list of projects in the plan which require external finance was handed to Mr. McNamara.^{2/} The external financing requested by SUDENE from abroad totals \$240 million over the next 3-4 years. This is to be attached to 25 projects with a total cost of \$475 million. With few exceptions, SUDENE is looking to the IBRD and the IDB to be the lenders. Thirteen of the projects are to be financed by IBRD loans totalling \$160 million. Of this amount, electric energy accounts for \$62 million, sanitation for \$50 million, irrigation and fisheries for \$28 million, and the USIBA steel plant in Bahia for \$28 million. No indication was sought or given that the Bank would take all of these projects under consideration.

Mr. McNamara indicated that Bank missions would soon arrive in Recife to have preliminary discussions on the irrigation and sanitation projects on the list. The Bank was certainly looking for

^{1/} Attached to the Operational Files copy of this memo.

^{2/} Copy contained in the files of Western Hemisphere "C".

opportunities to expand its operations in the Northeast, but it would be crucial that the projects in question have adequate rates of return.

A discussion ensued on the magnitudes of the resources being transferred into the Northeast from the southern and central parts of the country. Figures given by various SUDENE representatives were conflicting. Nevertheless, it seems that at present the annual inflow amounts to about \$550 million. Of this about \$100 million is provided for under Article 34/18, another \$250 million are tax resources transferred from the Federal Government to the states and municipalities in the area, and the balance of \$200 million consists of the excess in the area of federal expenditures over federal revenue collections.

Beyond this point, the discussion was essentially a dialogue between Messrs. McNamara and Rubens Vaz da Costa, and focused on the 34/18 scheme. Until recently, disbursements of 34/18 funds was slow. During the last 12 months, however, disbursements have sharply accelerated and the 34/18 cash balances deposited at the Bank of the Northeast are rapidly declining. This is occurring even though the inflow of funds is growing at an annual rate of 7-8 percent. One reason for the acceleration is that SUDENE is now restricting to one year the time limit up to which corporations elsewhere in the country can select freely from a SUDENE approved list the projects in the Northeast to which they want to attach their 34/18 funds. After one year, SUDENE is now dictating the selection of such projects. Another reason is that efforts are being made to increase the allocation of 34/18 funds to agricultural projects. Such allocations have so far been negligible (about 3 percent of total allocations).

In addition to the incentives derived from Article 34/18, industrial plants in the Northeast are given duty exemptions on imports not subject to the Law of Similar, i.e., of raw materials and equipment not being produced in Brazil. On top of that, income tax exemptions are granted for a period of 10 years after the starting up of industrial plants. Pioneer industries are fully exempt. So-called new industries receive a 50 percent tax reduction. Other industrial plants can claim 25 percent. Moreover, many industrial firms borrow at the Bank of the Northeast at negative real interest rates (the nominal rate presently is about 14.5 percent as compared with an inflation rate of 25 percent).

Mr. Vaz da Costa emphasized that there is no Government interference with the pricing of industrial products in the Northeast. He conceded that without the BNB's lending at negative real interest rates, industrial profits would be reduced. They would, however, not be wiped out.

SUDENE officials explained that they are trying to obtain modifications in prevailing U.S. income tax laws. These modifications would aim at enabling U.S. investors in the Northeast to benefit from

the above tax exemptions. Under the present double taxation treaty between Brazil and the U.S., any reduction of income tax payments in Brazil is offset by a corresponding increase in U.S. tax liability.

The discussion then turned to the question of the food deficit in the Northeast. Sample figures compiled by FAO indicate that the average per capita calorie intake in the Northeast is only about 1,350 per day as compared with 2,700 calories in the rest of Brazil. For the daily vitamin A intake, the figure for the Northeast is about 1,060 as compared with 4,000 for Brazil as a whole. On balance, a calorie deficiency of 25-30 percent is indicated.

In reply to questions by Mr. McNamara, the SUDENE officials stated that the problem facing the Northeast in education are indeed severe. Even though in the last nine years enrollment in elementary schools has doubled and in secondary schools and universities even tripled, in 1966 only 53 percent of children in the 7-11 age group attended school. The corresponding percentage for the average for Brazil is 60-68 percent and for the State of Sao Paulo 76 percent. In the 11-14 age group only few children attended school in the Northeast, whereas in the State of Sao Paulo about 75 percent are attending. Even though SUDENE is trying its best to help expand the educational facilities in the Northeast, this is of necessity a slow process if the present quality of education is to be maintained.

cc: Mr. McNamara (through Mr. Steckhan)
Mr. Diamond
Mr. Evans
Mr. Ballantine
Mr. Husain

GKWiese:mr

OFFICE MEMORANDUM

TO: Memorandum for Record

FROM: Gunter K. Wiese

SUBJECT: BRAZIL: Meeting of Mr. McNamara with
Governor of State of Bahia, LUIZ VIANA

DATE: November 18, 1968

Confidential

On October 24, Mr. McNamara met with Governor Luiz Viana. Also present were Mr. Angelo Sa, Industrial Secretary of the State, and three other assistants, as well as Messrs. Alter, Clark and Wiese. The Governor requested Bank help in four fields: (a) palm oil expansion, (b) rubber plantations, (c) tube wells, and (d) education. He handed over pre-feasibility studies on these projects.^{1/} The palm oil project would be carried out by a subsidiary of Volta Redonda, the leading Government steel company, and would be supported by a State credit program. Neither palm oil nor rubber prices were subsidized. Mr. Alter informed the Governor about the forthcoming Bank/FAO agricultural mission and assured the Governor that the mission would look at the first three projects. The Governor explained that he would hope the tube well project to concentrate on dry area cultivation of beans, corn, rice and other domestic food crops. In the more humid parts of the dry area, some of the wells might be used for cattle raising. The project would be scattered over 80,000 square kilometers and have a total cost of \$13 million.

Turning to education, the Governor emphasized that 22 percent of the States' expenditures is for education. These expenditures would increase by 2 percentage points per year until a level of 30 percent has been reached. The problem of education is serious in the State. In the 7-11 age group, one-third of the children are not enrolled, and almost 85 percent are not enrolled in the 12-16 age group. Any expansion of the education facilities would, however, have to be preceded by teacher training. While AID had financed some school construction in the State, they had run out of money and teacher training had not been included in their program.

Finally, the Governor handed over a small paper outlining an approach by the State to population control. However, even though the project would be camouflaged under the name, "prophylactics of abortion," it seemed impossible to get any State funds allocated to it.

^{1/} After reading them briefly during the following night, we shipped them to Washington where they have just arrived.

cc: Mr. McNamara (through Mr. Steckhan)
Mr. Evans
Mr. Ballantine
Mr. Hawkins
Mr. Husain

GKWiese:mr

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: November 18, 1968

FROM: Gunter K. Wiese *GKW*

SUBJECT: BRAZIL: Meeting of Mr. McNamara with
Mr. Lelio Toledo Piza, President of the State Bank of Sao Paulo
Mr. Vidigal, President of the Banco Mercantil, Sao Paulo
Mr. Walter Lorch, President of a Trucking Firm, Sao Paulo

On October 25, Mr. McNamara met socially with the above gentlemen. Also present were Messrs. Alter and Wiese. The conversation turned out to be somewhat one-sided; Mr. Vidigal spoke most of the time.

Little was said worth recording. All Brazilians present emphasized that profitability of Sao Paulo industries varies a great deal and that the shortage of working capital is a major handicap. Mr. McNamara indicated that the Bank is aiming at an increase not only in its general lending to Brazil, but also in its lending for Brazilian industry. He added that we are still groping to find a proper channel. A major obstacle for the Bank is the prevailing practice of certain government agencies to lend at negative real interest rates.

Mr. Lorch pointed out that additional problems confronting Brazilian industry are the obsolescence of much of the installed machinery, poor transport and poor communications. Many industries in Brazil are inefficient producers. This explains the high protective tariff system in the country. Moreover, in the past three years, drastic changes in the credit policy of the Federal Government had forced the entrepreneurs to cope with sizeable fluctuations in stocks.

There seemed to be consensus that the development of a capital market in Brazil might result in shifting capital from consumption into investment.

Turning to the situation and prospects of Brazil's railroad network, Mr. Lorch described it as being poor, obsolete, old-fashioned in mentality, and run like government agencies. Not only is the average operating ratio 200, but service is poor. Only high value merchandise travels by rail. Railways presently carry only 10 percent of domestic traffic; 80 percent moves by road and the balance by coastal shipping. Mr. Lorch added, however, that recently there had been a noticeable improvement in railway operations.

There was also consensus that lack of education facilities in Brazil in general, and in Sao Paulo in particular, is a major obstacle to development. There are only 200,000 high school students in the State. The situation in primary education is equally unsatisfactory.

cc: Mr. McNamara (through Mr. Steckhan)
cc: Messrs. Diamond, Sadove, Ballantine, Husain

GKWiese:mr

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: November 18, 1968

FROM: Gunter K. Wiese

~~Confidential~~SUBJECT: BRAZIL: Meeting of Mr. McNamara with President of the BNB
(Bank of the Northeast), RUBENS VAZ DA COSTA

On October 25, Mr. Vaz da Costa called on Mr. McNamara in Salvador. Also present were Messrs. Alter and Wiese. He briefly explained the current operations of the BNB. The total of outstanding loans presently amounts to NCr 800 million. By the end of 1969, this should grow to NCr 1.2 - 1.3 billion. At present the BNB is holding \$150 million of undisbursed 34/18 balances which are being used for short-term commercial credit operations. The majority of BNB stock is held by the Federal Government, but its capital was recently increased from NCr 15 million to NCr 100 million. Most of the additional stock was sold to private shareholders, which thereby increased from 2,000 to 10,000. As a result, the total capitalization of the BNB now amounts to NCr 175 million. Loans totalling \$50 million had, over the past years, been obtained from the IDB.

About 25 percent of BNB's lending is going to agriculture and the balance largely to industry and commerce. In the agricultural field, the development of livestock and of small irrigation reservoirs seems to be most promising. The nominal interest rate for agricultural loans was still 13 percent, which is negative in real terms. However, an increase to 18 percent is expected as at January 1969.

Industrial loans are now made at a 14 percent nominal interest rate. Efforts to raise this rate made by the Bank have so far proven unsuccessful. Mr. Vaz da Costa deemed this unfortunate because it overencourages the use of scarce capital and discourages growing utilization of relatively abundant labor. Basically, the pattern of industrial development in the Northeast which was sparked off by the inflow of rapidly growing 34/18 funds has in recent years been one of substituting imports from the south of the country. Most of the opportunities for import substitution had, however, by now been exploited and, in the future, emphasis would have to be given to developing industries which could export into the south or even to foreign countries.

Although the tempo of development in the Northeast is impressive, Mr. Vaz da Costa felt that it was not well balanced since the infrastructure is lagging. A pronounced trend to urbanization in the Northeast is creating especially difficult problems in a number of cities.

He then quoted a number of figures which showed that population growth in the Northeast is essentially going into urban unemployment. In 1960, 54 percent of a labor force totalling 12 million people was employed in agriculture, 13 percent of the labor force in industry, and 33 percent in service. The latter category included a substantial number of unemployed or semi-employed people. By 1985, it is probable that only 38 percent of the labor force, then likely to total 18 million people, would work in agriculture, 15 percent in industry and 47 percent in service.

cc: Mr. McNamara (through Mr. Steckhan)
cc: Messrs. Diamond, Takahashi, Husain

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: November 15, 1968

FROM: Gunter K. Wiese ~~Confidential~~SUBJECT: BRAZIL: Meeting of Mr. McNamara with
President of BNDE, JAYME MAGRASSI SA

On October 23, Mr. McNamara, accompanied by Mr. Alter and Mr. Wiese, called on Mr. Magrassi Sa. The latter summarized briefly the current operational activities of the BNDE. He then described a number of changes about to be introduced. In the future, the BNDE would actively promote new lending operations rather than passively wait for customers to come to the Bank, as in the past. The BNDE would establish the following lending priorities: (a) projects in the industrial sector which would help remove capacity gaps resulting in idle capacity elsewhere; (b) new lines of industrial production; and (c) integrated projects in the agricultural sector. He explained that BNDE's lending volume is growing rapidly and progressively shifting to lending for private sector projects. During the 21 months following January 1967, the BNDE has lent as much as during the preceding 15 years. In real terms, its commitment rate is expanding at about 10 percent per annum. Total annual commitments would probably reach \$300 million equivalent in 1968, plus an additional \$100 million in guarantees. Unfortunately, however, the BNDE could do little to help relieve the acute shortage of working capital in Brazil's industry. Its statutes require it to be a lender for fixed assets only.

Mr. Magrassi Sa then confirmed that at present the bulk of BNDE's funds is lent at a rate of about 22 percent per annum which, at the present rate of inflation of about 25 percent per annum, is negative in real terms. He attempted to justify this practice by the high tax burden on Brazilian industry. It became apparent that he is one of the eminent opponents in the Government to eliminating subsidized interest rates. He claimed that, on the average, industrial costs in Brazil consist of 10 percent wages, 27 percent financial costs and 23 percent of taxes.

Since BNDE is deeply involved in the USIMINAS and COSIPA steel projects, there followed a discussion of the competitiveness of Brazilian steel manufacturing and the current level of steel prices. In early 1967 steel prices had been raised by 20 percent and on October 1, 1968, by another 10 percent (during the same period inflation has been running at over 40 percent). Present import duties were 23 percent on carbon steel and 40 percent on special steel. The former rate gave adequate protection but the latter was still too low to permit the industry to compete with imports. Present capacity of Brazil's steel industry is about 4 million tons of ingots and is projected to grow at 15 percent per annum over the next few years. An

interesting information he disclosed was that the BNDE is planning to finance a new Government steel plant near Tubarao. The mill is scheduled to begin production in 1972. (The Bank-sponsored steel survey recommended against such a mill.) The mill is slated to produce 2 million tons, of which one million tons would be for domestic consumption and the remaining one million tons for exports, principally to Japan, Germany and France.

Finally, Mr. Magrassi Sa suggested cooperation between the BNDE and the IBRD in three fields: (a) big projects, (b) credit programs such as FINAME and FIPEME, for a multiplicity of projects, and (c) lines of credits for the importation of farm equipment not produced in Brazil. Most of the latter would have to be purchased in the United States and would help substantially to increase agricultural productivity.

cc: Mr. McNamara (through Mr. Steckhan)
Mr. Diamond
Mr. Fuchs
Mr. Husain

GKWiese:mr

DECLASSIFIED

SEP 19 2012

CONFIDENTIAL

WBG ARCHIVES

Meeting with Messrs. Brito/Camara of Journal do
Brasil

Saturday, October 26, 1968

Both expressed great pleasure at your visit and at Brazil
being "back in the Bank."

What help does Brazil need?

1. Above all Agriculture: "the country which has a good food supply will count as rich". Brazil could be absolutely self-sufficient and very well fed.
2. Education; but no good helping till the educational machine is improved. The education system is alienated from modern Brazil. Reform should start at the top; at Universities which are very old fashioned and European. Teachers at all levels are underpaid and so moonlight.
3. Politics. (Brazil must help itself here). There is a political crisis because Costa e Silva is not good enough. Army is very worried by inefficiency of Government and may change it. Such a change would be to the right. Chance of a change to the left very small (though Simonsen said 2/3 of Church is now left wing, and so are many students).

[I had to leave at this point in conversation to look after Silva]

me

WDClark:sf

DECLASSIFIED

SEP 19 2012

CONFIDENTIAL

WBG ARCHIVES

Meeting with Mario Simonsen of Vargas Institute

Saturday, October 26, 1968

The gravest problems are:

1. Inflation, but symptoms worse than disease, i.e. inflation rate is falling, largely because of good crops.
2. Population which stops real economic growth, and the finding of jobs for all.
3. Education. An appalling system - 60% flunk out at first grade and get no more education ever.
4. Savings. The habit is lost.
5. The 34/18 plans are far too capital intensive. SUDENE not good on agriculture and does not encourage entrepreneurs.
6. Railroads have very bad management and bad labor unions which are truckled to.
7. Politics. Weak leadership at top so each Minister has absolute power; President does not coordinate or guide policies.



WDClark:sf

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CONFIDENTIAL

SEP 19 2012

WBG ARCHIVES

Meeting with Mr. Luiz Silva - Saturday, October 26,
1968

Priorities

1. Agriculture. "A farmer in Brazil is a man who owns land, not one who makes it produce". Agriculture must be modernised.
2. Housing (he had been Minister of Housing). Home ownership essential to stability. Present programme is keeping up with population in small towns, but not in megalopolises. Sale is usually by mortgage at 4-10%.
3. Education very important indeed "but not of course for Bankers".
4. Labour Unions are part of state structure and wages are largely settled by lawyers in court; not market.
5. Politics. Weak at the top.



WDCClark:sf

OFFICE MEMORANDUM

CONFIDENTIAL

TO: Mr. Robert S. McNamara

DATE: October 31, 1968

FROM: William Clark *WMC*SUBJECT: Notes on Conversation with Editorial Directorate
of Estado do Sao Paulo

Father Mesguido spoke most and was translated by the eldest of three sons present. His first point:

The present Government is really trying to deal with the country's ills, as have both Governments since the Revolution (against Goulart in 1964). Its attack on inflation has brought it down to about 25% per annum.

The armed forces run the Government but are essentially democratic in spirit, though the laws passed are often totalitarian. The country would be a tyranny if the laws were rigidly enforced, but it is more of an anarchy because they are not, e.g. an opposition member of Congress (Alves by name) has criticised the armed forces, an act punishable under law; the President does not wish to act, but the junior officers are trying to make him.

The students have no right to form associations but they do and the Government sometimes acts with sudden severity and sometimes lets it go.

There is a serious political crisis, but it seems unlikely to explode at present.

In the NorthEast, they agreed with you, the crisis is over food and education. But "they started from zero and they feel that the Government has begun to bring them forward" therefore there is again no explosive crisis.

The Archbishop of Recife (Camaro) has said that you are dividing the country North versus South. The Bishops meeting in conclave have denounced your (American) intervention in the question of birth control.

Father Mesguido then went on to say how much every one resented the superior air of indifference adopted by the U.S. to Latin America. "If the U.S. could realise how it could use Brazil as a bridge to the Spanish speaking South American countries, it could solve all our problems".

The main problem, it was agreed, was inflation, which had not been conquered and could easily destroy Brazil. There is virtually no unemployment in Sao Paulo (they showed pages of help wanted ads) yet the negotiations on wages and salaries were proceeding peacefully which was hopeful.

WDClark:sf



by foreign savings in their various forms -- grants, loans and technical assistance.

The saying goes that when everything runs well with São Paulo the country will go the same way. São Paulo provides 52% of the country's federal revenue. It means that more than half of the funds for all federal investments are originated in this State. It means that more than half of this giant development effort now being carried on in the less privileged areas of Brazil -- especially the Northeast -- emanates from São Paulo. In the other hand, according to the latest figures made available by the Northeast Development Superintendency (SUDENE), 56,89% of the private investment made in the Northeast, in accordance with the federal laws on fiscal incentives, derived from Paulista private enterprise.

However, at the present time São Paulo is under the threat of having its own development rate substantially reduced, which would consequently prevent the maintenance of its present rate of assistance to the other States.

This happens because São Paulo is now going through a critical stage -- either we expand the economic infra-structure and fundamental public utilities, already definitely below standards, raising them to a level compatible with the continuity of its present industrial development, or we will face a crisis which might lead us to a complete collapse.

After World War II São Paulo, which already was the most developed area of Brazil, witnessed an industrial boom. Consequently the State went through a stage of fast urbanization (the urban population jumped from 52.8% in 1950 to 62.8% in 1960 and above 70% now), due to the migration of large segments of the Brazilian rural population toward the Paulista urban areas, especially the capital's Metropolitan Area.



GABINETE DO GOVERNADOR
DO
ESTADO DE SÃO PAULO

Despite the fact that our birth rate (State of São Paulo) is the lowest in the country, the State presents the top, or just about the top population growth, exactly on account of the entrance of Brazilians from other areas. From a peak of 35.62 births per 1.000 inhabitants, in 1.954, the rate went down to only 27.57, in 1.967. This is a complete reverse from the national trend.

This shows that the Paulista people is definitely striving for controlled parenthood, although such effort is overcome by a different trend from across the border. And it would be unfair to penalize Paulistas for something beyond their control, for striving to counterbalance a national trend.

The excessively fast urban growth in the State prevented public utilities from keeping pace with it. Similar problem affected the expansion of the school system, which has not been able to provide the specialized technical labor required by the industrial development.

We have exhausted now all possibilities of postponement in the elimination of this disparity between the urban industrial development, in one side, and the economic infra-structure and public utilities in the other. Previous administration in the State invested heavily our savings in economic projects; we must now maintain such investments and invest heavily in the social sector. Therefore, it is indispensable that São Paulo should obtain immediately the financial resources to carry on some undelayable projects.

We would like to mention, in first place, those referring to water supply and the expansion of the sewer network in Metropolitan Area of the capital. The present population of over 7 million (5.7 million at the City Proper), is now growing at an yearly rate in excess of 6%. Quite possibly it may triple by the nineties.

An American specialized firm (Hazen and Sawyer Engineers, New York), which studied the city's water and sewer problems, stated on July, 1967:



GABINETE DO GOVERNADOR
DO
ESTADO DE SÃO PAULO

"São Paulo and the surrounding communities face a water supply and sewage disposal crisis. Less than 60% of the population of the Metropolitan Area is served by a public water system.

"At the present time only about 35% of the people in the Metropolitan Area are connected to public sewers".

It would be interesting to remind that, by 1970, according to present programs, 70% of the Northeastern urban population may have adequate potable water supply. The State of São Paulo, which is providing a high share of the funds for their development programs has not yet achieved such rate!

Regarding transportation, the picture is not too different. São Paulo's Metropolitan Area is an important national crossway in all directions. This shows how vital is the city's beltway, whose final alignment has been selected by the consulting firms Parsons, Brinckerhoff, Quade & Douglas, associated with Edwards and Kelcey, Inc., and Brazilian company, under contract with GEIPOT, within the general agreement with the World Bank. Preliminary budget and feasibility report has been completed and are already available. Final report will come shortly.

A similar case is the new highway linking the São Paulo area to the seashore, whose projects are being submitted to the same consultants with the same purpose.

All these projects are within a transportation master plan which the above consultants are preparing for the whole State of São Paulo.

During a seminary at Jackson, Miss., on February last year, sou stated that the technological gap between the under-developed and the developed nations can be bridged only if attacked from its root: education. You added that the technological advance, which depends entirely from a high level of general knowledge and management competence, can be achieved only through that on which progress stands: the education of the young and the old.



GABINETE DO GOVERNADOR
DO
ESTADO DE SÃO PAULO

We agree with you completely. Education and health enjoy top priority in my administration. We are investing here in São Paulo, in education, almost the same amount invested by the Federal Government all over the country -- this fiscal year a record 28% of our budget, and next year 30%. And we are giving top priority to the technical schools of the medium level -- our bottleneck -- so as to enlarge the specialized labor required by the industrial development of the State and the Nation. Last, but not least, education means a controlled rate of population growth, although at a long range.

Also, the State's growing urbanization has deprived the rural areas from agricultural labor. Consequently, we urgently need to improve farming techniques in the State, to counter-balance this reduction through higher productivity, exactly as it happened in your country. We are carrying on a global agricultural policy -- rural electrification, basic health, mechanization, agricultural vocational schools, etc -- aiming not only at higher productivity but also at settling the people in the farming areas.

The consumption of electricity in the State is growing steadily, now at an annual rate above 10% and, in order to avoid a harmful rationing of power, São Paulo must add 3,739,000 kW to its installed capacity before 1977. Centrais Elétricas de São Paulo (CESP) has cleared several projects, including their feasibility reports. Some of these projects have been submitted to the World Bank for study.

Regarding water and sewage, education and agriculture, we have already prepared several projects, including their reports on technical and economic feasibility, which we would like to submit to you, should there be any financing possibility.



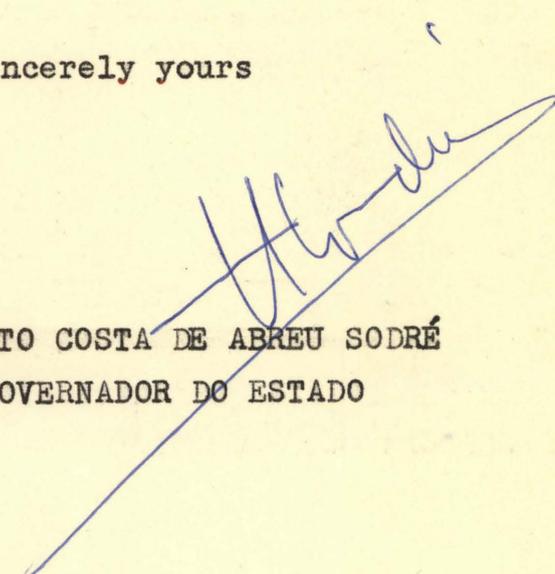
GABINETE DO GOVERNADOR
DO
ESTADO DE SÃO PAULO

These are some of the critical areas to which we especially call your attention. We hope that the World Bank may cooperate with us, not only for the solution of the problems herein mentioned, but others, almost equally important.

We have already proved that we are able to accept and fulfill the terms of the World Bank's loans, such as happened in the past in regard to the hydroelectric projects of Salto Grande, Jurumirim and Chavantes, for instance.

We would welcome the opportunity of going deeper in the analysis of all the above mentioned subject, here in São Paulo, or in the United States, at any time we may have the privilege of enjoying your company and learning from your experience, under less time pressure.

Sincerely yours



ROBERTO COSTA DE ABREU SODRÉ
GOVERNADOR DO ESTADO

COCKTAIL PARTY OFFERED BY MR. LUIS VIANA FILHO
GOVERNOR OF THE STATE OF BAHIA, FOR MR. ROBERT
MCNAMARA, ON THURSDAY OCTOBER 24, 20:30 - AT
THE PALACIO DA ACLAMAÇÃO, SALVADOR .

Boris Tabacof	Secretary of Finance, State of Bahia
Angelo C. de Sá	Secretary of Industry and Trade, State of Bahia
Luis Prsco Viana	Secretary of Information, State of Bahia
Hilton J. M. Rodrigues	Chief of Governor's executive office (Casa Civil)
Helio R. de Brito	Private Secretary of the Governor
Lelivaldo Brito	President of the State Bank
Victor Gradim	Member of ^{1/} Reconcaço Development Comission ^s , former President of the Development Bank
	<u>1/</u> Reconcaço: Salvador and surrouding area.

LUNCH HOSTED BY MR. DELFIM NETO, MINISTER OF FINANCE
FOR MR. ROBERT MCNAMARA, ON WEDNESDAY OCTOBER 23RD
AT 13:15 - AT THE YATE CLUB OF RIO DE JANEIRO

Helio Beltrão	Minister of Planning
José Magalhães Pinto	Foreign Trade Minister
Mario David Andreazza	Transport Minister
Afonso Albuquerque Lima	Interior Minister
José Costa Cavalcanti	Mines and Energy Minister
Francisco Negrão de Lima	Governor of Guanabara State
Roberto de Abreu Godré	Governor of São Paulo State
Israel Pinheiro	Governor of Minas Gerais State
Ivo Silveira	Governor of Santa Catarina State
Ernani Galvêas	President of Central Bank of Brazil
Nestor Yost	President of Bank of Brazil
Ary Burger	Director of Central Bank of Brazil
Paulo Pereira Lira	Director of Central Bank of Brazil
Jayme Magrassi de Sá	B.N.D.E. President
João Paulo dos Reis Veloso	General Secretary - Ministry of Planning
Mario Bhering	President of ELETROBRAS
Lucas Garcez	President of CESP
John Cotrim	President of FUR NAS
João Camilo Pena	President of CEMIG
Cicero Sales	President of COCAP

Marcus Vinicius de Moraes	Special Assistant to the President
José Maria Vilar de Queiroz	Advisor to the Finance Minister
Elizeu Rezende	Director of D.N.E.R.
Sergio Bath	Secretary to Foreign Affairs - Planning Ministry
Rodrigo Ajace Moreira Barbosa	General Secretary - Transport Ministry
Ary Pinto	Advisor to the Finance Minister
José Flavio Pecora	Advisor to the Finance Minister
Gustavo Silveira	Press Officer - Finance Ministry
Oscar Victor Peterson	President of ALCOMINAS
Mario Trindade	President of Banco Nacional de Ha- bitação
Luis Clovis de Oliveira	President D.N.P.V.N. (Departa - mento Nacional de Portos e Vias Navegáveis)
Ambassador Jorge Alvares Maciel	Assistant Secretary to the Ministry of Foreign Affairs
Milton Ferreira	Chief of Cabinet - Ministry of Planning
Isaac Lopes de Castro	Advisor to the Planning Minister
Rafael Aduino Costa	Press Officer - Planning Ministry
Antonio Adolfo Manta	President Rêde Ferroviária Federal

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: December 11, 1968

FROM: Gunter K. Wiese *GW*SUBJECT: Visit by Mr. Herbert Levy, Secretary of
Agriculture, State of Sao Paulo, December
12, 1968

We have no knowledge of any operational matters that Mr. Levy might raise at this meeting. He was, as you will recall, present at your meeting with Governor Abreu Sodre in Sao Paulo on October 25, 1968 (see my memorandum of November 19, 1968 which is attached).

As you know, we are presently considering two projects in the State of Sao Paulo for Bank financing: namely, Sao Paulo Water Supply and Sewerage, and Sao Paulo Beltway. The former project is the first phase of a long-term expansion project; its cost estimated at US\$150-160 million which would, on the basis of our cost sharing formula in Brazil, justify a Bank loan of some US\$60 million. Our lending for this project would, however, be dependent upon the findings of an economic mission which in March 1969 will study the finances and investment program of the State of Sao Paulo (see Mr. Alter's memorandum to you dated December 3, 1968). Were we to go ahead with the project, our timetable forecasts an appraisal mission for September/October 1969.

The second project, the Sao Paulo Beltway, is of more than local importance since it would also improve interstate traffic. The feasibility report is due in March 1969. The project cost is presently estimated at some US\$130 million and a Bank loan of US\$50 million is envisaged. We are planning to send a mission to review the feasibility study in March 1969 and were we to decide to process the project, an appraisal mission is scheduled for March 1970.

You will also recall that we have been considering a grain silo project in the Port of Santos. The project is delayed because of the Transport Minister's decision to change the location of the silo to a presently undeveloped area. Last week we suggested to Mr. Delfim Neto that he initiate a reconsideration of this decision. We have not yet had a reply. Mr. Levy is well acquainted with this matter. Grain exports from the State are presently being held back due to lack of silo capacity at Santos.

Attachments (2)

President has seen

Biographical Data

Herbert Victor Levy born November 2, 1911, founded Banco da America in 1943 of which he is a director. He has been professor of Brazilian Economy at the University of Sao Paulo. Mr. Levy is probably best known as a politician. He was for many years Sao Paulo State Congressman in the Federal Assembly. He belonged to the National Democratic Party (U.D.N.) of which, during one period, he was President. Together with Carlos Lacerda, he represented the more conservative right wing of that party. U.D.N. was, as were all political parties, abolished in 1965 and Mr. Levy then joined ARENA, the pro-government party, when it was formed in 1966. During his time as Congressman, Mr. Levy, spoke particularly for the rural interest groups in the State of Sao Paulo.

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: November 19, 1968

FROM: Gunter K. Wiese

ConfidentialSUBJECT: BRAZIL: Meeting of Mr. McNamara with
Governor of State of Sao Paulo, ABREU SODRE

On October 25, Mr. McNamara, accompanied by Messrs. Alter and Wiese, called on Governor Abreu Sodre. Also present were: Luis Arrobas Martins, State Secretary of Finance; Herbert Levy, Secretary of Agriculture; Eduardo R. Yassuda, Secretary of Public Works; Firmino Rocha de Freitas, Secretary of Transport; Lelio Toledo Piza, President of the State Bank; and Lucas Nogueira Garcez, President of CESP (the largest power company in the State, which is also a Bank borrower).

The Governor initiated the discussion by presenting some salient facts on the economy of the State which he called the dynamo of Brazil. The level of unemployment in the State at present is low. Its average per capita income is about \$500. It produces 52 percent of all federal revenue and 57 percent of the 34/18 funds flowing into the Northeast. Its urban population amounted to 53 percent in 1950, 62 percent in 1960, and now accounts for 70 percent of the State's population. Although the State has a low birth rate, the progressive urbanization of the State materialized because of migration from other States. Over the last 13 years, the birth rate in the State had declined from 35.6 per thousand to 27.7 per thousand. Nevertheless, the infrastructural capacity is falling rapidly behind. The Governor said that the metropolitan area of Sao Paulo is growing at an annual rate of 6 percent.

The Governor then requested IBRD assistance for the following sectors:

1) Water Supply and Sewerage in the Sao Paulo Metropolitan Area

The present population of Sao Paulo of about 7 million people is expected to triple by 1990. Only 60 percent of the area is presently served by the water system and only 35 percent is connected with sewerage facilities. He deemed it ironic that by 1970 roughly 70 percent of the urban areas in the Northeast may be connected while Sao Paulo, unless something drastic is done, would certainly show a much lower percentage. Investment in sanitation should certainly have top priority.

2) Education

The Governor considered this a second priority for the State investment program. At present, the State is spending 28 percent of its

revenues on education - as much as the country as a whole. He is planning to raise this percentage to 30 percent next year.

3) Agricultural Projects

He did not elaborate on this.

4) Electric Energy

Power consumption in the State is growing at a rate of over 10 percent per annum. He then had Mr. Lucas Garcez hand over an official application for Bank loans for three power projects to be carried out by CESP, i.e.,^{1/}

- (a) Capivara (requiring an external loan of about \$60 million).
- (b) Promissao (an external loan of perhaps \$30 million may be required).
- (c) Agua Vermelha (which would probably need an external loan of about \$100 million).

5) The Sao Paulo Beltway (no further comments were made)

6) The Sao Paulo Railway (no further comments were made)

7) The new Santos Freeway (no further comments were made)

The Governor emphasized that despite its relatively high per capita income, the State of Sao Paulo is still in dire need of external capital. The State provides 52 percent of the federal revenue but receives back only 1.2 percent. Only a small fraction of federal expenditures goes to the State. In reply to a question by Mr. McNamara, he said that he expected present tax rates in the State to continue. This is essentially a question of the tax rate of the turnover tax - now at 17 percent - which produces 96 percent of the Sao Paulo State revenue. He considered this level already too high to render any additional increase feasible and in this context alluded to widespread tax evasion in the State.

Mr. McNamara indicated that he was fully convinced that the need for more infrastructure in the State is indeed sizeable, but that it appeared still more manageable than the need in the Northeast of Brazil. Mr. Alter added that the recent constitutional reform had resulted in an increasing flow of resources to the states and municipalities at the expense of the Federal Government. What was needed from the point of view of Brazil as a whole was to shift more investment functions and responsibilities back to the States. The Secretary

^{1/} A reply is being prepared in the Bank.

of Finance pointed out that the total expenditures of the State were already at a level of NCr 4 billion a year. He conceded that an increase in the 17 percent turnover tax by, say, 2 percentage points, would raise over NCr 400 million of additional revenue, which would go a long way toward solving some of the infrastructure investment problems in the State. He reiterated, however, that the 17 percent sales tax rate had to be considered a maximum feasible under present circumstances.

cc: Mr. McNamara (through Mr. Steckhan)
Mr. Sadove
Mr. Knox
Mr. Ballantine
Mr. Husain

5

12/15
 Susp = for Reminder
 12/16

FORM NO. 75 (2-60) INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
 INTERNATIONAL FINANCE CORPORATION INTERNATIONAL DEVELOPMENT ASSOCIATION

ROUTING SLIP		Date Nov. 7 th
NAME		ROOM NO.
Mr. Stecker		
Mr. McNamara:		
Do you wish to see Mr. Winters?		
to lunch with Mr. W.?		
RBS 11/7		
To Handle		Note and File
Appropriate Disposition		Note and Return
Approval		Prepare Reply
Comment	X	Per Our Conversation
Full Report		Recommendation
Information		Signature
Initial		Send On
REMARKS		
<p>If at all possible I would appreciate an answer before Mr McNamara leaves on his trip.</p> <p>Any of the following dates would be convenient to Mr. Winters:</p> <p><u>Dec. 5th, 9th, 10th, 13th or 16th.</u> 12:30</p> <p>Thank you 11/15, 12/16 for lunch</p>		
From	K. Gwinner. <i>[Signature]</i>	

OFFICE MEMORANDUM

TO: Mr. Rainer B. Steckhan

FROM: Kenelm Guinness *K.G.*

SUBJECT: Visit of President of Brazilian Light
and Power Company

DATE: November 7, 1968

I received a telephone call from an old friend of mine, Mr. Lars Bengston, in Toronto today. Mr. Bengston was for many years a member of the legal staff of the Bank and is now General Counsel to Brazilian Light and Power Company.

Mr. Bengston asked me to enquire whether it might be possible for Mr. Robert Winters, the new President of Brazilian Light and Power Company, to meet Mr. McNamara during his forthcoming visit to Washington in early December. He would like to discuss Brazil in general, and his Company's investment plans in Brazil in particular. You will recall that Brazilian Light and Power Company has been a substantial borrower of Bank funds. I think Mr. Winters would be particularly pleased to be invited to lunch with Mr. McNamara.

No specific date has been fixed for Messrs. Winters and Bengston's visit and it could, I understand, be arranged to some extent at Mr. McNamara's convenience.

KGuinness:mc

RESUME

The Honorable Robert H. Winters

President, Brazilian Light and Power Company - 1968

Nationality: Canadian

Age: 58

Masters in Electrical Engineering at MIT

- 1948 Minister of Reconstruction and Supply
- 1949-53 Minister of Resources and Development
- 1953-57 Minister of Public Works
- 1957-65 Chairman, Rio Algom Mines Ltd.
Chairman, Atlas Steels Co. Ltd.,
Chairman, Newfoundland Corporation
- President, Vice President and Director of numerous
companies, including Ford and IBM
- 1966-67 Minister of Trade and Commerce
- 1968 President, Brazilian Light and Power Company
and Director of numerous companies

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: April 7, 1969

FROM: Andrew M. Kamarck *AK*SUBJECT: Visits of Deputy Director General of FAO and Executive Director
of International Coffee Organization

Mr. Oris V. Wells (American), Deputy Director General of the FAO, and Mr. Alexandre Beltrao (Brazilian), who is Executive Director of the International Coffee Organization and also Executive Director of its Coffee Diversification Fund, are visiting the Bank for meetings on April 8 and 9.

Both are members of the steering committee of the Joint FAO/IBRD/ICO Coffee Study. I am the Bank representative on that committee.

In addition, Mr. Beltrao will participate in a meeting at the Bank on Wednesday, April 9, to discuss his plans with regard to the national coffee production goals of the member countries of ICO and the activities of the Coffee Diversification Fund.

Mr. Beltrao has specifically asked to pay a courtesy call on you. Brief biographical notes are attached.

*9:20 wed 4/9
Called 4/8*

President has seen

BIOGRAPHICAL NOTE

ALEXANDRE F. BELTRAO

Born: April 28, 1924

Place of Birth: Curitiba, State of Parana, Brazil

Academic Life: Graduated as a civil engineer from the University of Sao Paulo in 1948. Subsequently undertook post-graduate study on the economics of industrial and business management at the University of Brazil, Rio de Janeiro. Beginning in 1951 he spent two years in Europe studying regional and economic planning development.

Professional
Career:

On his return to Brazil Mr. Beltrao worked as Director of a firm of Consultants and carried out a wide range of studies in Brazil in the field of industrial and agricultural development, including a study of the Brazilian coffee economy.

From 1962 onwards Mr. Beltrao has been closely associated with international coffee affairs. He attended the 1962 United Nations International Coffee Conference as an observer for the State of Parana. He was named special adviser to the chairman of the Brazilian Coffee Institute (IBC) in 1964; was head of IBC's office in New York from 1965 to 1967; was chairman of the World Coffee Promotion Committee of the International Coffee Organization in 1965-66; was chairman of Pan American Coffee Bureau in New York from 1965-67; and was a Brazilian delegate to the various meetings of the ICO between 1964-67.

Mr. Beltrao was appointed Executive Director of the International Coffee Council in 1968. In that capacity he is also Executive Director of the newly established Coffee Diversification Fund of the ICO.

Mr McNamara
to see
see 2/17

OFFICE MEMORANDUM

TO: Memorandum for the Record

DATE: February 17, 1970

FROM: Gerald Alter *GA*SUBJECT: Meeting of Mr. McNamara with the Minister of Interior
of Brazil, Col. José Costa Cavalcanti

Minister Cavalcanti of Brazil paid a courtesy call on Mr. McNamara on Monday, February 16. He was accompanied by the new Brazilian Ambassador, Mr. Gurgel Valente; Mr. Rubens Vaz da Costa, President of BNB; and Mr. Kafka. Messrs. Knapp and Alter were also present. Mr. McNamara expressed his satisfaction with the more recent pace of development in the Northeast of Brazil and congratulated the Brazilians on their approach to the problem. He observed that there were several projects in preparation which would benefit the Northeast, and he hoped that the Bank could continue to give support to Brazil in this area. Questions were then raised concerning certain weak points in the picture, particularly with respect to the extent of illiteracy, nutritional problems and distribution of income.

The Minister raised the question of IDA credits for projects in Northeast Brazil. Mr. McNamara pointed out that we had always approached the problem of access to IDA from the point of view of the country as a whole, not particular regions. We took into account, of course, what the country was doing to correct deficiencies in the poorer parts of its territories and the impact of these efforts on the country's overall economic position. IDA resources at the present time, however, were severely limited and we had been unable to provide IDA assistance to Brazil, given other claims. With a higher level of total resources, hopefully to be obtained from the third replenishment, we hoped to be able to do more in Latin America.

The Minister left a letter and some supporting material relating to irrigation projects in the Northeast.

cc: Mr. Wiese o/r
Mr. Husain o/r

resident has seen

SUGGESTED REMARKS AT THE SIGNING OF THE PROPOSED
\$25 MILLION LOAN TO BANCO DO NORDESTE DO BRASIL

I am extremely pleased to sign with you this loan for the development of the Northeast of Brazil. We hope that this will be the first in a series of loans for projects in the Northeast and other less developed parts of the country. Through these projects we would hope to assist your Government in bringing the fruits of development closer to people who have not fully participated in the very rapid growth of Brazil's economy.

I would like to take this opportunity to express our recognition of the very sincere efforts of the Government of Brazil to invest funds and manpower to develop the Northeast, and some of the results of this effort are already apparent in the rapid growth of industrial and agricultural production. My colleagues and I have been very closely following your Government's efforts and we hope that the Bank's resources will be linked with productive ventures in this region. Towards this end we worked with your Government in studying the transport sector in Brazil. This study has given rise to a large number of projects suitable for World Bank financing. We hope that the proposed loan for highways, which we propose to present to the Executive Directors within the next two months, will include \$50 million for highways in the Northeast. Recently we sent a large mission to study agriculture in the Northeast and we hope that in the next few months we shall discuss this report and its recommendations with your Government as a basis for future Bank projects.

Let me assure you, Mr. Minister, that the Bank will continue and, if necessary, strengthen its efforts to work with your Government in finding and implementing projects which would add to the production and employment opportunities in the less developed parts of your country.

DESCRIPTION OF THE LOAN TO BNB

Borrower: Banco do Nordeste do Brasil S.A.

Guarantor: Government of Brazil

Amount: The equivalent in various currencies of \$25 million.

Approved by Executive Directors: January 20, 1970.

Purpose: To enable the Borrower to finance the foreign exchange costs of industrial projects of private enterprises in the Northeast of Brazil.

Amortization: In semi-annual installments expected to begin on February 15, 1973, and end on February 15, 1987. Payments will be based on a composite amortization schedule made up of the amortization schedules of the individual sub-loans financed under the project.

Interest Rate: Seven percent.

Commitment charge: 3/4 of 1 percent.

Relending: The prior approval of the Bank is required for individual sub-loans exceeding \$250,000. Bank funds are to be relented by BNB to ultimate borrowers at not less than 9½ percent; the foreign exchange risk to be borne by the ultimate borrower.

Special Provisions: BNB has agreed to:

- a. Apply to its operations a formula, satisfactory to the Bank, defining its maximum exposure in long-term, medium-term and short-term lending in accordance with its different resources, to assure a satisfactory degree of liquidity.
- b. Limit its total indebtedness to ten times the amount of its unimpaired equity and its outstanding term debt (with initial maturities of more than one year) to four times its unimpaired equity.
- c. Undertake all action that may be necessary to ensure (a) that its annual return (in real

terms) will not drop below 5% of its equity and (b) that the return on capital invested in BNB's industrial lending program will not drop below a rate equal to the Bank's lending rate on the proposed loan.

- d. Make arrangements to enable it to draw on supplementary resources in the case its ordinary resources are insufficient to carry out its program of long-term industrial lending.

BRAZIL BASIC ECONOMIC DATA

Area: 8,512,000 square kilometers
3,286,000 square miles

Population: 92.3 million (est.; mid-1969)
Growth rate 3.0% (estimate)

Gross National Product in 1968 (preliminary):

At market prices: NCr 91.7 billion (\$27.0 billion); per capita NCr 1,026 (\$302).
At factor cost: NCr 73.3 billion (\$21.6 billion); per capita NCr 820 (\$242).

<u>GDP Growth Rates:</u>	1968 GDP by Sector of Origin (est.):	<u>Financing Invest- ment in 1968:</u>	million % of NCr's GNP
1947-1962 6.0%	Agriculture 31%	Investment	13,288 14.5
1962-1964 2.6%	Industry 31%	National Savings	11,780 12.8
1964-1967 4.5%	Services 38%	Current Acc't. Bal.	1,504 1.7
1967-1968 7.6%			

<u>Government Finance:</u>	<u>Consolidated Public Sector billion NCr</u>	<u>% of GDP</u>	<u>Federal Gov't. Budget billion NCr</u>	<u>% of GDP</u>
Current Receipts (of which taxes)	29.2 (27.3)	31.5 (29.5)	10.3 (9.8)	11.1 (10.6)
Current Expenditures	20.8	22.5	7.3	7.9
Savings	8.4	9.0	3.0	3.2
Investment Expenditures	9.1	9.8	4.2	4.5
Deficit	.7	.8	1.2	1.3

<u>Money, Prices & Exchange Rates:</u>	<u>Money Supply (private sector)</u>		<u>General Price Index (Dec. 1964 = 100)</u>		<u>Exchange Rate (selling rate)</u>	
	<u>million NCr</u>	<u>% Change</u>	<u>Index</u>	<u>% Change</u>	<u>NCr/\$</u>	<u>% Change</u>
December 1965	7,891	77.0	134	34.2	2.220	18.9
December 1966	8,801	11.5	187	39.1	2.220	-
December 1967	12,735	44.7	233	25.0	2.715	23.4
December 1968	17,849	40.1	293	25.5	3.830	41.1
December 1969	22,130	24.0	352	20.1	4.350	13.6

Balance of Payments in 1968 (million \$)

Exports (goods & services)	\$2,072
Imports " "	2,305
Resource Gap	-233
Interest Payments (net)	-180
Other Factor Payments (net)	-90
Donations (net)	60
Current Account Bal.	-443
Foreign Direct Invest.	54
M< Loan Disbursements	392
M< Loan Amortization	-286
Net Short Term Credit	412
Other Transactions	-150
Decline in Official Reserves (+)	21

Merchandise Exports (fob) in 1968

	<u>mil. \$</u>	<u>percent</u>
Coffee	801	42.4
Cotton	131	6.9
Iron Ore	107	5.7
Sugar	102	5.4
Cocoa	72	3.8
All Other	677	35.8
Total	1,890	100.0

External Debt on Dec. 31, 1968:
(outstanding and disbursed)

Medium & Long Term	\$2,736.5
Short Term	1,082.8
Total	3,819.3

Debt Service Ration in 1968: 22.5%
(excl. amort. of short term credits)

Official Reserves (Oct. 31, 1969):

Net International Reserves \$388 million
Gross International Reserves \$914 million

Loans from IBERD at Dec. 31, 1969:

Outstanding & Disbursed	\$198.8 mil.
Undisbursed	284.1 "
Total	\$482.9 "

OFFICE MEMORANDUM

TO: Mr. Robert McNamara

DATE: February 12, 1970

FROM: Gerald Alter *GA*SUBJECT: BRAZIL: FORTHCOMING VISIT OF THE MINISTER OF THE
INTERIOR, COSTA CAVALCANTI

1. The following is background information for your meeting with Col. Jose Costa Cavalcanti, Minister of the Interior, Brazil.
2. Col. Jose Costa Cavalcanti has been the Minister of the Interior since January 1969 when he replaced General Albuquerque Lima. Previously, from 1967 to 1969 he was Minister of Mines and Energy. He is fifty-one years old and a native of Fortaleza, in the Northeast of Brazil. Until 1962, Col. Cavalcanti made his career in the Brazilian army. In 1962 he was elected to the Federal House of Representatives where he chaired the commission on National Security. He participated actively in the preparation of the 1964 military coup d'etat as a liaison agent between dissident civilian and army elements. Following the coup he was appointed President of the Commission on National Security.
3. Col. Cavalcanti has cooperated fully with the Bank, both in the Ministry of Mines and Energy and in the Ministry of the Interior. The latter supervises the Federal program for the development of Brazil's less developed regions, including the Northeast. In his former capacity, Col. Cavalcanti supported the Bank's efforts to ensure that the power companies earn an economic return on their investments and to promote the execution of well studied and coordinated investment programs in the sector. As Minister of the Interior, he has backed BNB's President, Mr. Vaz da Costa, and has refrained from interfering in BNB's day-to-day management and individual lending decisions. However, it is too soon to make any comments about Col. Cavalcanti's impact on the development of the Northeast.

Brazil - Northeast

1. The Northeast has one-third of Brazil's population and covers one-fifth of its land area. It was Brazil's first area of large-scale colonization. Cane sugar for export, cultivated by slaves imported from Africa, was the basis of its prosperity in the sixteenth and seventeenth centuries. By the Eighteenth Century, its position in the sugar trade had been superseded by more efficient producers located in the Caribbean islands. Within Brazil, the Northeast fell into increasing isolation, as first gold in Minas Gerais and then coffee in Rio and Sao Paulo attracted the attention of the Central Government, brought in European immigrants, led to the penetration of the hinterlands and laid the basis for agricultural and industrial production for domestic consumption.

Brazil: Forthcoming visit of the Minister of the
Interior, Costa Cavalcanti

February 12, 1970

2. When industrialization began as a process of import-substitution, sparked by the two World Wars and deliberately promoted by the Central Government since 1947, the Northeast had neither the markets nor the technical and managerial skills needed to participate. In fact, its relative backwardness increased as regional savings (primarily from sugar, cocoa and tobacco production) flowed into more profitable investments in the Southeast and, as its terms of trade deteriorated when more expensive manufactures from the Center-South replaced formerly imported foreign articles, while its agricultural exports were penalized by the persistent over-valuation of the cruzeiro.

3. Population pressure in the coastal areas of the Northeast has resulted in migratory flows within the Region towards the hinterland and the larger cities, and outside the Region primarily towards the Southeast, and the frontier areas of the North and Center-West. The major obstacles to settlement of the hinterland have been generally poor soils, periodic droughts and inadequate transportation facilities. Until 1961, when a special program of Government tax benefits was introduced to induce Center-South corporations to invest in the Northeast, industrial development was insufficient to contribute significantly to the absorption of urban labour, constantly swollen by migration from the countryside. Emigration to areas outside the Northeast has played a major role in alleviating population pressure; despite very high natural growth rates, the Northeast's population increased by 2.2 percent p.a. in the sixties compared to 3 percent for Brazil as a whole.

4. Prior to the late fifties, the Central Government's efforts to aid the Northeast took the form of public works programs for victims of periodic droughts and investments in reservoirs. This assistance was largely ineffective since it was sporadic and uncoordinated and failed to tackle the major obstacles to the Northeast's development; namely, inadequate infrastructure, including education and health services, low level of agricultural productivity, and lack of industrial development.

5. The establishment in 1959 of the Superintendency for the Development of the Northeast (SUDENE) marked the start of a major, long-term Federal development program for the Northeast. This has taken the form of direct Federal investments in infrastructure, tax transfers to the Northeastern State Governments, expanded credit from official institutions and tax rebates on private investment in Northeastern industrial and agricultural projects.

Brazil: Forthcoming visit of the Minister of the
Interior, Costa Cavalcanti

February 12, 1970

6. The transfer of resources to the Northeast from the rest of the country has been sizeable; in 1968 it was estimated at over 10 percent of the regional gross domestic product. The immediate impact has been on the improvement of the highway network and on the rise of industrial investment. The former, by opening up the more humid and fertile areas of the hinterland, notably Maranhao, has contributed to a sharp increase in agricultural output and relieved population pressure in the congested coastal areas. Industry's contribution to the expansion of aggregate output should rise over the next few years as the large number of industrial projects financed under the 34/18 system (corporate tax rebates for investments in Brazil's less developed regions) reach the operative phase.

7. The Northeast's per capita product is now estimated at \$200 and that of Brazil at \$300. From 1958 to 1966, the Northeast's product is estimated to have grown at an annual rate of 7 percent substantially higher than the Region's 4.5 percent p.a. growth during 1949-58 and exceeding Brazil's 5.4 percent p.a. growth in 1958-66. It would be premature, however, to conclude that this improved performance corresponds to a new stage of self-sustained growth. The most dynamic sector of the Northeast's economy in recent years has been agriculture, which grew by 9 percent p.a. compared to only 5 percent p.a. for industry. Yet, according to the findings of a mission sent by the Bank to survey agriculture in the Northeast, the growth of agricultural output has derived primarily from greater use of land and labour and not from improved productivity. While this pattern of development has contributed to alleviating the unemployment problem, it has not made a significant contribution to a shift from subsistence to commercial-type agriculture capable of generating savings and absorbing new techniques.

8. SUDENE's fourth development plan contemplates expenditures of NCr \$6,900 million (about \$2.0 billion) during the five-year period 1969-73. The targets envisage annual investment expenditures by SUDENE of roughly twice the actual spending rate during the preceding three-year plan period. The proposed sectoral distribution of total investment and direct SUDENE expenditure is as follows:

	<u>Sudene</u> (In NCr\$ million of 1968)	<u>Total</u> ^{1/} (1968)	<u>Sudene</u> (Percentages)	<u>Total</u> ^{1/} (Percentages)
Power	270	1,250	19	18
Transportation	190	1,160	14	17
Water & Sanitation	150	660	11	9
Natural Resources	120	210	9	3
Human Resources	165	1,830	12	27
Agriculture	240	1,100	17	16
Industry	60	60	4	1
Other	175	640	13	9
Total	<u>1,370</u>	<u>6,910</u>	<u>100</u>	<u>100</u>
(in \$)	(403.4)	(2,034.7)		

^{1/} Federal and State Governments, development banks and external agencies.

Brazil: Forthcoming visit of the Minister of the
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February 12, 1970

9. Following the previous major emphasis on industrialization, the current plan marks a shift towards a more balanced approach which will entail substantial investments in infrastructure, such as electric power, transportation and education. Although industrialization will continue to be an important objective, the Government is aware that the problems of employment and growth cannot be tackled by a lopsided emphasis on industry alone. The latter has contributed little to the reduction of unemployment and the absorption of manufactures will require rising agricultural productivity and income. As regional import-substitution reaches its rational limits, the future emphasis in industrialization should be on catering to the expansion of the Northeast market as well as on exports to the more developed areas of Brazil and abroad. Consequently, SUDENE intends to be more selective in its approval of projects submitted under the 34/18 system. This is in consonance with the recommendations of a recent Bank study on the Northeast's industrialization which found that, while there were no obvious misallocation in investments, the criteria for approving projects needed to change according to the changing nature of markets for Northeastern products.

10. With respect to agriculture, while there continues to be some emphasis on irrigation, there is growing recognition of the role of credit and extension services, more intensive use of land in the coastal belt and adjoining hinterland and settlement of the more humid and fertile frontier areas both within and outside the region.

11. A combination of high levels of industrial investment and improved agricultural productivity, supported by the intensive development of transportation, education and sanitation, could result in a continued economic growth rate of the order of 7 percent p.a. If, however, per capita income levels are to approach those prevailing in the more prosperous regions of Brazil in the foreseeable future, emigration from the Northeast to the industrial Southeast and to the largely empty lands of the North and Center-West will have to play a major role. The continued rapid growth of other parts of Brazil is a prerequisite for both the absorption of Northeast labour and the transfer of resources to the Northeast.

Proposed Bank Lending in the Northeast

12. SUDENE's current development plan envisages external financing of about \$110 million in 1970-72. However, our last economic mission identified projects in the Northeast to which external financing in the amount of about \$384 million could be attached. Of these projects, the ones being considered by the Bank could lead to lending of about \$250 million. As in the rest of Brazil, an informal division of labour is developing between the Bank and AID. The concentration of Bank lending would be on transport, agriculture and industrial credit,

Brazil: Forthcoming visit of the Minister of the
Interior, Costa Cavalcanti

February 12, 1970

while AID is emphasizing urban development and development of human resources. The IDB is the main source of external financing for power projects.

13. Our current lending program for Brazil includes the following Northeast projects in fiscal years 1970-72.

	<u>1970</u>	<u>1971</u> (In \$ million)	<u>1972</u>
Agricultural credit (ENB)		30	
Sao Francisco Irrigation		8	
Maranhao Settlement			10
Agriculture (unidentified)			25
Highways (included in highway projects)	52	35	25
Port of Recife			4
Industrial credit (ENB)	<u>25</u>		<u>35</u>
Total	<u>77</u>	<u>73</u>	<u>99</u>

Transportation

14. We are attempting to include in our future transportation loans all economically feasible highway and port projects emerging from the recent Bank-UNDP financed transportation survey. The second highway project will be submitted to the Executive Directors in March-April. We do not see any major difficulty in continuing the highway program in FY 1971 and 1972 and the preparation of the project is under way. In FY 1972, depending on the results of a feasibility study now being prepared, we may finance part of the cost of modernizing Recife, the Northeast's major port.

15. We expect that our financing for the highways will be a major contribution to the improvement of transportation facilities within the Region and between the Northeast and the other regions of the country. Attaching our financing to highways would also commit substantial Federal resources to the development of the Northeast since all the domestic financing would be made available by the Central Government. Development of the Port of Recife will be an important step in the overall improvement of the Northeast's coastal shipping services. Their present poor quality adds appreciably to the input costs of the Region's agriculture and industry.

Agriculture

16. Our first agricultural project in the Region will probably be for agricultural credit through BNB. An appraisal mission is scheduled for April. A major policy issue with respect to agricultural credit would be the introduction by the Government of positive interest rates for agricultural credit; the current maximum interest rate for

Brazil: Forthcoming visit of the Minister of the
Interior, Costa Cavalcanti

February 12, 1970

agricultural loans is 18 percent and the rate of inflation is about 20 percent. Until now, the Government has resisted our suggestions that its agricultural interest rate policy be changed. We shall, however, attempt to arrive at a satisfactory agreement with the Government on a policy to introduce positive rates before we negotiate the proposed loan for agricultural credit.

17. The Agricultural Sector Survey Mission which visited Brazil from October 19 to December 14, 1969, is preparing several reports on its findings. A special consultant team focused on Northeast agriculture. Its preliminary conclusions is that, although there is considerable scope for labour-intensive, capital-saving means to increase agricultural productivity, agriculture alone does not hold the key to the Northeast's unemployment problem. The latter must be tackled through a combination of agricultural development, industrialization, public works, emigration and family planning.

18. Among the agricultural mission's recommendations which may eventually mature into projects eligible for Bank financing are the rehabilitation of the cacao areas, development of the cashew industry, greater use of fertilizers and new seeds, development of livestock in the dry areas, modernization and diversification of the sugar cane plantations, expansion of agricultural credit and extension services, establishment of agricultural processing industries and related storage, handling and packaging facilities. Considerable emphasis is placed on the importance of improving transportation, in particular feeder roads, coastal shipping and ports. On the other hand, support for irrigation projects should proceed on a moderate scale where soil conditions are suitable and the projects promise an adequate economic return. It is also suggested that while settlement of the frontier areas of Goias, Mato Grosso, Maranhao and Amazonia should be actively encouraged, this should take the form of agricultural credit and technical assistance rather than heavy investments in planned "colonies".

Industrial Credit

19. The EMB industrial credit was approved by the Bank's Board on January 20 and is expected to be signed on February 16. It will provide foreign exchange for the new industries being set up under the fiscal incentives program and should be the first tranche of a series of such loans.

20. Simultaneously, we will be discussing with the Government improvements in the current system for the selection of industrial projects and improvements in the allocation of credit which could lead to an increase in the flow of private resources from the more developed parts of the country to the Northeast.

8

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: June 2, 1970

FROM: Gerald Alter *gh*

SUBJECT: Meeting of Mr. McNamara with the Minister of Finance of Brazil, Mr. Antonio Delfim Netto and the Minister of Mines and Energy, Mr. Antonio Dias Leite

Minister of Finance Delfim Netto and Minister of Mines and Energy Dias Leite met with Mr. McNamara on Monday, May 25. They were accompanied by Mr. Mozart Gurgel Valente, Ambassador of Brazil; Mr. Henrique Rodrigues Valle, Ambassador to the OAS; Mr. Paulo H. Pereira Lira, Director of the Central Bank; Mr. Jose Maria Villar de Queiroz, Advisor to the Minister of Finance; and Mr. Alexandre Kafka, Executive Director of the IMF. Messrs. Knapp and Alter were also present. The major topics considered were interest rates in agriculture, the need for Bank assistance in the storage program in agriculture, the steel sector, and possible Bank participation in projects in the mining sector.

With respect to interest rates in agriculture, the Minister explained that Brazil was now willing to accept the application of ex post monetary correction to agricultural credits with a maturity of 5 years or more. Mr. McNamara welcomed this move toward positive interest rates in the agricultural sector. There was some discussion of the problems which arise from the present system of applying various rates of interest, some of which were clearly negative, to loans of less than 5 years. The Minister took the position that the dangers of misallocation, arising from very low or negative real interest rates in the case of loans for the financing of equipment, were not great. It was decided that there would be additional discussions between the staff and the Brazilian authorities on the problem. At a subsequent meeting between the Finance Minister and Mr. Alter, the Minister agreed that the Brazilian Government would review the system of interest rates applicable to loans of less than 5 years in the agricultural field, with a view to determining whether the system was conducive to promoting adequate utilization of loans with a longer maturity bearing full monetary correction. This subject would then be discussed with the Bank during appraisal.

In the case of agricultural storage, the Minister of Finance emphasized their need for Bank assistance in formulating a program. He stressed the relationship of an agricultural storage program to the stabilization program, pointing out that it was extremely difficult to stabilize prices with the short-run fluctuations in agricultural prices attributable to the lack of storage facilities. It was agreed that the Bank's agricultural sector mission, which was scheduled to discuss its report with the Brazilian authorities in the next few days, would follow up on this matter.

President has seen

June 2, 1970

The Minister touched briefly on the continued interest of the Brazilian authorities in obtaining financial support from the Bank for their steel expansion program. The Minister himself is interested in developing private steel plants to operate alongside the public enterprises in this sector, in order to be able to judge better the efficiency of the public enterprises. He would be interested in eventual Bank support for such a project. He also mentioned, for the short-run, the COSIPA and USIMINAS expansion program. Mr. McNamara indicated that in the steel sector, the Bank should very clearly be considered a lender of last resort and he hoped the Brazilian authorities would make an effort to obtain the great bulk of financing from other sources.

The Minister of Mines and Energy outlined some of the minor iron ore projects in the planning stage, pointing out the very great contribution that these projects would make to Brazil's balance of payments. He confirmed that the MBR project, already being considered by the Bank, has the full support of the Brazilian Government. He mentioned the very large project, now being planned in association with U.S. Steel, implying that the Brazilian authorities would be in touch with the Bank at a later date. He asked for a fairly early reaction to the idea of Bank support for the current program of the Companhia de Vale do Rio Doce. They need to double the track on which ore is carried and they need to expand the port. While they expect continued financial support from other financial institutions such as Ex-Im of Japan and the Kreditanstalt, there are certain items of equipment amounting perhaps to 1/3 or 1/4 of US\$110 million which they would like to purchase on the basis of international competition and would appreciate Bank assistance for this reason. On the basis of a subsequent conversation with Mr. McNamara and Mr. Knapp, Mr. Alter informed the Minister in a later meeting that, given the other project needs in our lending program for 1971-72, the expansion of the current Rio Doce program did not seem attractive to us. The Minister seemed to understand the reasons given for this decision.

There was also some discussion of Brazil's debt servicing problems and of the study now being completed, on the basis of which the Brazilian authorities intend to establish a firm program. They emphasized that they have already instituted effective controls over short-term debts, and would be having discussions within Brazil with the various agencies to formulate a debt management program covering the longer term debt. They promised to make available the study to the Bank in about one month.

cc: Mr. Knapp
Mr. Wiese
Mr. Husain

GAlter:pa.

of Minas Gerais. He is 40 years old, is a graduate civil engineer and has a Doctorate in Mathematics from New York University.

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: May 22, 1970

FROM: Gerald Alter *gla*SUBJECT: BRAZIL: Your Meeting with the Minister of Mines and Energy

Brazil's Minister of Mines and Energy, Mr. Antonio Dias Leite, is coming to attend the signing of the Marimbondo loan. He is meeting you immediately after the signing ceremony. We have not been informed as to what subjects he would like to discuss with you; however, he may be interested in the following:

1. Iron Ore Mining and Export

The Minister was formerly the President of the government-owned Cia. do Valle do Rio Doce (CVRD). The company is a well managed one and the biggest exporter of iron ore from Brazil (about 17 million tons per year). Its expansion program has hitherto been financed from bilateral sources. Recently, the company entered into a partnership with US steel to exploit the vast iron ore resources in the Amazon region. The Minister has, in the past, expressed interest in obtaining World Bank financing for the project and we have included it in the lending program for fiscal 1974.

Iron ore promises to be one of the best prospects for increase in Brazil's foreign exchange earnings. Our lending program also includes the MBR iron ore project, a joint venture of Hanna Mining Co. and the Brazilian Antunes group, for a loan of \$50 million in fiscal 1971. If the Minister raises the question of financing iron ore projects beyond 1971, we should express our readiness to consider suitable projects. We would, however, wish to see that all necessary efforts are made to obtain suitable bilateral financing especially if large imports of equipment are envisaged. ✓

2. CVRD's Industrial Program

The CVRD has also been preparing a program for the establishment of paper and plywood plants to improve employment opportunities in the Rio Doce Valley in Minas Gerais. They hope to associate foreign firms, particularly in Scandinavia, with these ventures. The CVRD has expressed interest in obtaining Bank assistance for these projects but has not so far submitted any concrete proposals. If suitable plans are prepared, Bank or IFC should be prepared to consider these.

3. Electric Power Sector

A detailed investment and financing program has been prepared for the power sector requiring external financing of about \$750 million on power projects during 1970-73. Of these, projects including the Marimbondo, requiring financing of about \$250 million, are proposed to be submitted to

President has seen

Mr. Robert S. McNamara

- 2 -

May 22, 1970

the World Bank. We have informed the government that larger projects, like the Marimondo and the Sao Simao (scheduled for fiscal 1972), would be submitted to joint financing. For fiscal 1971, we have scheduled a loan of \$50 million for Osorio project in the extreme south of Brazil. The project is small and will be executed by a new company (Eletrosul), requiring substantial supervision. It is, therefore, not proposed to submit this particular project for joint financing. It appears that Brazilians would be able to meet their remaining external financing needs from other multilateral and bilateral sources.

cc. Messrs. Knapp
Alter
Fuchs
Paterson (IFC)

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara (Through Mr. Knapp)

DATE: May 22, 1970

FROM: Gerald Alter *GA*SUBJECT: BRAZIL - Background Information for Your Meeting with the Finance Minister and for the Mid-term Review of the Country Program Paper

1. We have written this memorandum as a background for your meeting with the Brazilian Finance Minister, and for the mid-year review of the country program you had asked for. In it we have briefly summarized the findings of the economic mission (back to office report attached) and reviewed the current state of the lending program.

I. Recent Political Developments

2. Brazil continues to be governed by the Armed Forces. The new President was inaugurated in October 1969; his term of office runs to March 1974. Although he has expressed the intention of returning the country ultimately to representative government, severe limitations on the political activities of the Opposition continue. The biggest uncertainty about the Brazilian scene is whether a transition to constitutional government can be made peacefully.

3. Elections for State Governors are scheduled for the end of the year and the Government Party has nominated official candidates. Although there will be Opposition candidates, the Government's candidates are likely to win. On the whole, the Government has tried to select competent non-political personalities to contest these elections.

4. Except for the Ministry of Industry and Commerce, the Government's economic team has remained intact since the change of government and the basic policies to stimulate economic growth, improve the balance of payments position and combat inflation continue. The Finance Minister, Antonio Delfim Neto, is the head of the economic team, and is said to be the most influential non-military member of the Cabinet.

II. Recent Economic Developments and Important Economic Issues

5. Brazil experienced rapid economic growth in the last two years; GDP increased by about 8 percent in 1968 and 9 percent in 1969. For the first time in many years economic expansion has created new employment opportunities equivalent to the increase in the labor force - about one million per year. There has been a sharp improvement in the balance of payments position; in 1969 exports increased by 23 percent and imports by only 8 percent. The net foreign exchange reserves increased by \$80 million in 1969.

6. The continuing improvement in the economic environment is in large measure the product of skillful economic management by the Government. However, in the last three years the Government has had little success in reducing

President has seen

Mr. Robert S. McNamara (Through Mr. Knapp)

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the rate of inflation significantly; this has stayed at the rate of 20 to 25 percent and is expected to be about 20 percent this year. The main constraint on the Government's ability to achieve further rapid progress in reducing the rate of inflation is its belief that any sharp curtailment of demand would be too costly in production and employment and probably intolerable politically and socially. The Finance Minister has given top priority to maintaining a high level of economic activity and his chief policy instrument has been generous expansion of credit to the private sector. This has been made possible by the success which the public sector has had in generating substantial savings through high rates of taxation and, lately, some effective control of non-military expenditures.

7. The following are some of the major issues which the Government faces in the area of economic policy.

(i) External Capital Flows and Debt Management

8. The Brazilians are using the substantial improvement in their balance of payments position to build up external reserves. They have maintained the policy of flexible exchange rates and extension of incentives to stimulate non-traditional exports. While the recent high coffee prices and increase in non-traditional exports provides the Brazilians with an excellent opportunity to strengthen their liquidity position, there remains the need to mobilize large amounts of capital - of the order of \$1 billion in commitment of medium and long term loans per year - for external debt service, and import requirements of a 6 to 7 percent growth rate. The economic mission's preliminary analysis suggests that in the seventies and the eighties Brazil could support service on its existing and new debt provided that about 20 percent of the new capital were available on concessionary terms, another 30 percent available on terms similar to those of the World Bank and the remaining from suppliers. Some lengthening of the average repayment period for supplier credits would be required; recently the average repayment period was only six years.

9. During discussions on the last Country Program Paper some questions arose about the projected capital flows to Brazil and the country's creditworthiness for about a \$1 billion a year in the commitment of medium and long term loans. Subsequently, on February 11, we submitted to you a memorandum on Brazil's external debt and Bank risk. Our conclusion was that although Brazil's need to borrow was substantial, the prospects were that Brazil would continue to be able to service its external debt. We also concluded that allocation of IDA funds would somewhat ease Brazil's debt servicing burden. The findings of the recent economic mission have strengthened our analysis. The trend in coffee prices and growth of non-traditional exports will strengthen Brazil's external reserves and hence its ability to meet temporary liquidity problems.

10. The Brazilians are preparing an external financing and debt management program which the Finance Minister proposes to discuss with you. As you are aware, he and other members of the Government strongly oppose a Consultative Group. It is my judgment that at this time pressure from us on

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the Government to agree to a Consultative Group would be counter productive. We should emphasize to the Finance Minister that we are concerned more with the substance of coordination than its form. If Brazil can formulate a rational external financing program, which would seek to mobilize foreign capital in amounts and on terms consistent with Brazil's development potential and debt servicing capacity, and can obtain suitable financing for this program, there would be no reason for the Bank to insist on a formal Consultative Group.

(ii) Inflation

11. The need for a further reduction in the rate of inflation still exists, even though we do not consider it a sine qua non for Bank lending. While flexible price policies affecting the allocation of specific resources can substantially insulate the economy from the ill effects of inflation, the task of the economic managers in dealing with specific issues affecting these is rendered extremely difficult and complex. There is always the danger that a relaxation of some of the crucial policies, such as coffee taxation, could lead to an increase in the rate of inflation, making the problems of economic management and insuring price flexibility even more difficult. An important aspect of inflation in Brazil is that quasi automatic wage and price adjustment built into the economy tend to perpetuate the preexisting rate of inflation. Further progress in reducing inflation would, therefore, have to be the result of a containment in the public sector's demand on real resources, and there is no prospect of a substantial reduction in the near future.

(iii) Price Policies

12. In general, the Government has tried to ensure that prices affecting the supply and demand for specific resources are kept flexible and do not lead to large scale unplanned penalties or subsidies. Thus, the Government has maintained a flexible exchange rate policy and a policy of adjusting public utility tariffs to reflect the cost of services. However, the distortion of interest rates remains an important source of concern. Private banks and financieras supply short term funds with high interest rates - of the order of 12 to 26 percent in real terms - while Government institutions supply medium and long term funds on low and, in the case of agriculture, negative interest rates. In the case of industrial credit, the Government reformed its interest rate policy last year. Agricultural credit, however, continues to be furnished at nominal rates of 9 to 17 percent. The resulting subsidy to the farmers is indiscriminate and is largely a function of the rate of inflation. Banking institutions, furnishing agricultural credit, avoid decapitalization because they have access to interest-free Government funds. The system presumes that Government will continue indefinitely to generate a surplus in its accounts, part of which it can channel to agricultural credit at low or negative interest rates.

(iv) Investment and Financing

13. Certain sectors of the economy have lagged considerably in recent years and unless their financing and organizational problems are

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resolved quickly they may impede rapid economic growth. The two most significant cases are steel and telecommunications. In the steel sector the expansion program has lagged because of the lack of suitable domestic and foreign financing and because of the Government's policy of controlling steel prices. Brazil, with a rapidly expanding market for steel and one of the richest iron ore reserves in the world, may in the next few years have to import substantial quantities of steel. In telecommunications, although there has been some improvement in the last few years, the sector remains beset by inadequate organization, lack of suitable long term investment and financing plans, and excessive dependence on high cost domestic producers for telecommunication equipment. Unless the present policies change, telecommunications in the major urban centers may face a breakdown before long.

III. Lending Program

14. At the program review in December you decided that we should allocate staff for project work as though we were going to carry through fully the gross lending recommended in the Country Program Paper (\$1.7 billion for 1971-75). You also decided that net lending should be planned at \$250 million per year of which, starting in 1972, IDA would provide at least \$25 million. Our work is proceeding on this basis, although in our discussions with the Brazilians we have referred only to the possibility of Bank lending of about \$200 million a year. The Finance Minister is likely to raise with you the allocation of IDA funds for Brazil. You may wish to consider giving him some indication about this in view of the recent progress in discussions on IDA replenishment.] x

15. In the Country Program Paper we envisaged gross lending of about \$360 million in fiscal 1971. As project preparation and discussions with the Brazilians on important sector issues have proceeded, we have revised the program for 1971 and subsequent years. The Highway III (\$100 million), Sao Paulo Beltway (\$60 million) and the Industrial Credit (\$50 million) projects have slipped owing to a longer lead time required for project preparation than we had expected. We have decided not to proceed with the appraisal of the Northeast Agriculture Credit project (\$30 million) because we have been unable to reach with the Brazilians an agreement on the agriculture interest rate policy. On the other hand, the MBR Iron Ore project (\$50 million) and the Railway project (\$35 million) are now likely to be ready for lending in the coming fiscal year. The changes in the program for 1971 have been tentatively approved by the Chairman of the Loan Committee and we now expect that Bank lending to Brazil in fiscal 1971 will be of the order of \$200 million. (The revised lending program is attached.) It is possible that with some effort on the part of the Brazilians, the Highway III project (\$100 million), now scheduled for 1972, could be ready for a Bank loan in fiscal 1971. However, since this would raise Bank lending in fiscal 1971 to about \$300 million, we are not recommending that a special effort be made to bring this loan to the Executive Directors in the coming fiscal year. x

16. We are not proposing any major changes in the lending program before we formulate our country program later this year. The following is a brief

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review of lending in each of the sectors.

(i) Agriculture

17. Given Brazil's natural endowments, any significant increases in agricultural production would be the result of investment in infrastructure, such as transport and direct investments by farmers, rather than direct public investment in agriculture itself. Our agriculture sector program consists largely of credit projects, particularly in the Northeast. Although we have reached an understanding with the Government on the interest rate for the Bank's livestock project, in the absence of an understanding on agriculture interest rates in general, I would not recommend proceeding with these projects. Accordingly, we have deferred to 1972 the Northeast agriculture credit project formerly scheduled for appraisal this month. We shall continue our efforts to arrive at an understanding with the Government and shall maintain the existing agriculture credit projects in the lending program. If we are unable to proceed with these projects, our lending in the Northeast would be particularly affected because agriculture is a substantial part of our proposed operations in that region. In the meantime we would continue to process specific investment projects in the Northeast, such as the Sao Francisco irrigation project and the Maranhao settlement project.

(ii) Industry

18. After discussions with the Chairman of the Loan Committee, we are preparing for fiscal 1972 a project to provide financing for private investment banks, provided that they would raise complementary resources in the local capital market. We hope by this mechanism to stimulate the mobilization of private savings for medium and long term investments. Early next month we shall present to the Government specific proposals regarding this. During preliminary discussions the Finance Minister and the Central Bank have expressed considerable interest in our approach.

19. In the Northeast of Brazil we shall continue to channel our funds for industrial finance through the Banco do Nordeste do Brasil.

20. Work on a \$50 million loan for the MBR iron ore project in 1971 is in progress. The project will add about \$70 million gross a year to Brazil's foreign exchange earnings.

21. Soon after the completion of the Steel Study in 1966 the Government of Brazil had approached the Bank for financing steel projects. The Government was told that the Bank would consider financing steel projects only if it was unable to obtain suitable financing elsewhere. It has now been confirmed that such financing on suitable terms may not be available for all the projects in Brazil. The COSIPA steel project was included for a loan in 1972 in the country program we presented to you in December. Returns on marginal investment in this mill are about the highest in the industry since the plant was designed for 2 million tons (present capacity is less than 1 million tons) and a substantial infrastructure has already been built for

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this larger capacity. We shall proceed to prepare this project and shall also examine closely the Government's policies affecting the sector. In the next few months, we shall approach the Chairman of the Loan Committee with specific proposals regarding the project.

(iii) Education

22. As explained in the Country Program Paper, we would essentially leave to AID the external financing of this sector. A small project has been appraised for the current fiscal year. We shall keep ourselves apprised of developments in this sector to see if there is any justification for further Bank involvement.

(iv) Power

23. We hope to submit the major projects in the sector to joint financing as in the case of the Marimondo project. However, the project scheduled for fiscal 1971 is relatively small and will be executed by a newly established agency. We feel that this would not be suitable for joint financing and a Bank loan for the entire equipment component is scheduled.

(v) Transport

24. Transportation remains the biggest area of Bank activity in Brazil and through successive loans for highways, railways and ports we hope to support the Government's program of reform of the sector, particularly of the railways. We have included in the 1971 program a \$35 million loan for investment by the railways for the transport of iron ore complementary to the MBR project mentioned above. We hope that loans for the railway and the MBR projects can be made simultaneously. The loan for the railways would be conditional on the railways formulating a reform program which would give reasonable expectation of the elimination of the operating deficit of the Central, South-Central and the Southern systems by the middle of the present decade. We are assisting the railways in formulating such a program and are reasonably hopeful of reaching agreement on the outlines of a program by the time we are ready to negotiate this loan.

(vi) Telecommunications

25. The Bank has not in the past lent for telecommunications in Brazil and no telecommunication project is included in our program. However, the economic mission has come back with the finding that the sector is beset with problems of organization, investment planning and financing. We are taking a close look at the sector to determine the scope of Bank assistance and hope to be able to present a strategy for the Bank's participation in the telecommunications sector when we formulate the new Country Program Paper later this year. You may wish to ask the Finance Minister as to whether the Government would be prepared to discuss with the Bank issues of investment programming, organization and procurement affecting Bank financing of projects in the sector. In the past, the Government has been reluctant to submit telecommunication projects to international agencies, largely because

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it wanted to reserve procurement for domestic manufacturers.

(vii) Water Supply and Sewerage

26. A loan of \$30 million is scheduled for a Water Supply and Sewerage project in Sao Paulo for this fiscal year. Although we are not recommending any major Bank involvement in the sector, we may wish to follow up the present project with another loan for the same system in 2 to 3 years' time. We shall have more to say on this in the Country Program Paper.

Attachments (2)

cc. Mr. Knapp
Mr. Aldewereld
Mr. Friedman
Mr. Alter
Mr. Adler
Mr. Wiese
Mr. Knox
Mr. Diamond
Mr. Weiner
Mr. Evans
Mr. Ballantine
Mr. Avramovic
Mr. Husain

Population: 85.7 m
 GNP Per Cap: \$250

Iva. BRAZIL - 5 YEAR LENDING PROGRAM

		(\$ millions)							
		Fiscal Years				Total	Total		
		1970	1971	1972	1973	1974	1975	1964-68	1969-73
Agricultural Credit - BNB	IBRD			25.0					
Agricultural Credit	IBRD				60.0				
Agricultural Credit	IBRD						60.0		
Irrigation - Sao Francisco	IBRD		8.0						
Land Settlement - Maranhao	IBRD			10.0					
Agric. Unidentified	IBRD					30.0			
Agric. Unidentified	IBRD					30.0			
DFC - BNB I	IBRD	25.0							
DFC - BNB II	IBRD				35.0				
DFC - BNB III	IBRD						40.0		
DFC - Industrial Finance I	IBRD			50.0					
DFC - Industrial Finance II	IBRD					60.0			
Education	IBRD		10.0						
Iron Ore - MBR	IBRD		50.0						
Iron Ore - North	IBRD					50.0			
Steel	IBRD			50.0					
Power XXI - Marimondo	IBRD	80.0							
Power - Osorio and Capim Branco	IBRD		50.0						
Power - Sao Simao	IBRD			75.0					
Power - Itumbiara	IBRD					50.0			
Power - Agua Vermelha	IBRD						65.0		
Highways II	IBRD	100.0							
Highways III	IBRD			100.0					
Highways IV	IBRD				100.0				
Highways V	IBRD					100.0			
Highways VI	IBRD						100.0		
Ports I	IBRD		20.0						
Ports II	IBRD			10.0					
Railways I	IBRD		35.0						
Railways II	IBRD			20.0					
Beltway - Sao Paulo	IBRD			60.0					
Transp. Unidentified	IBRD				35.0				
Transp. Unidentified	IBRD				35.0				
Transp. Unidentified	IBRD						75.0		
Transp. Unidentified	IBRD						75.0		
Water Supply - Sao Paulo	IBRD		30.0						
	IBRD	205.0	203.0	400.0	265.0	320.0	415.0	291.1	1147.9
No.		3	7	9	5	6	6	10	27

** Note: Program to be reduced to --

250.0 250.0 250.0 250.0

DESCRIPTION OF THE SECOND HIGHWAY CONSTRUCTION LOAN

Borrower: Government of Brazil.

Amount: The equivalent in various currencies of \$100 million.

Approved by Executive Directors: March 31, 1970.

Purpose: To help finance:

- a) the construction and paving of eight Federal and State road sections totalling 872 km;
- b) the improvement and paving of nine road sections totalling 1,267 km;
- c) the detailed engineering and supervision of the proposed works;
- d) consulting services for the detailed engineering of 2,290 km and feasibility studies of 3,814 km of roads which could be included in future Bank highway projects; and
- e) consulting services to strenghten the Planning unit of the National Highway Department, and to improve construction supervision.

Amortization: In 25 years, including a 4 year period of grace, through semi-annual installments beginning September 1, 1974 and ending September 1, 1995.

Interest Rate: Seven percent.

Commitment Charge: 3/4 of 1 percent.

Special Provisions: The loan would be made to Brazil and the overall execution of the project would be the responsibility of the National Highway Department (DNER). Execution of the project would be the responsibility of DNER for federal highways and of the corresponding State Highway Departments (DERs) for state and/or delegated national highways. The Bank would sign project

President has seen

Special Provisions:
(cont'd.)

agreements with the states of Minas Gerais, Santa Catarina, and Rio Grande do Sul, as the DERs in these states would be responsible for the construction of state highways and/or delegated national highways. Prior to effectiveness the Federal Government would enter into subsidiary agreements, acceptable to the Bank, with the DERs of these states as well as with the DERs of the states of Espirito Santo, Parana, and Rio de Janeiro which would be responsible for detailed engineering and feasibility studies included in the project.

Contracts for construction and paving would be awarded on the basis of international competitive bidding. To take advantage of economies of scale through the use of larger contractors, some construction lots would be combined into packages and bidders would be given a choice to bid on packages or single lots.

Loan for
Marimbondo Hydroelectric Project

Approved by Executive Directors: May 19, 1970

Borrower: Central Eletrica de Furnas S.A.

Guarantor: Brazil

Amount: Equivalent in various currencies of US \$80 million.

Purpose: To help finance the Marimbondo hydroelectric plant and associated transmission facilities; additional generating units for the Furnas plant; and technical, training and management improvement services and related equipment.

Amortization: In 30 years, including 7½ years of grace, through semi-annual installments beginning September 1, 1977 and ending March 1, 2000.

Interest Rate: 7 percent.

Commitment Charge: 3/4 of one percent.

Special Provisions: To provide a legal framework for joint financing, the Loan Agreement provides that:

- 1) Furnas will make its best efforts to obtain and utilize joint loans for the Project.
- 2) The amortization schedule will be adjusted so that the combined repayments of principal on the proposed Bank loan and the joint loans would, insofar as practicable, not exceed the repayments that would have been necessary had the full external financing been provided by the Bank, but without reducing any principal installment due the Bank below \$100,000 or extending the final amortization date of the Bank loan.
- 3) The Bank has a right to premature the loan if any of the joint loans has been prematurely.

President has seen

BRAZIL BASIC ECONOMIC DATA

Area: 8,512,000 square kilometers
3,286,000 square miles

Population: 92.3 million (est.; mid-1969)
Growth rate 2.8% - 3.0% (est.)

Gross Domestic Product in 1969 (preliminary):

At market prices: NCr\$128 billion (US\$32 billion); per capita NCr\$1,388 (US\$342).
At factor cost: NCr\$106 billion (US\$26 billion); per capita NCr\$1,146 (US\$282).

<u>GDP Growth Rates:</u>		<u>1969 NDP by Sector of Origin (est.):</u>		<u>Financing Investment in 1969:</u>		<u>million NCr\$</u>	<u>% of GDP</u>
1950-62	6.9%	Agriculture	17%	Investment		22,516	17.6%
1963-66	3.1%	Industry	29%	National Savings		21,903	17.1
1967-69	7.4%	Services	54%	Current Acc't. Bal.		613	0.5

Treasury Budget Results in 1969:

	<u>millions of NCr\$</u>	<u>General Price Index (Dec. 1964 = 100)</u>		<u>Exchange Rate (selling rate)</u>	
		<u>Index</u>	<u>% Change</u>	<u>NCr/\$</u>	<u>% Change</u>
Current Receipts	13,953	134	34.2	2.220	18.9
Total Expenditures	14,709	187	39.1	2.220	-
Deficit (-)	-756	233	25.0	2.715	23.4
(deficit equals 0.6% of GDP)		293	25.5	3.830	41.1
		352	20.2	4.350	13.6

Money, Prices & Exchange Rates:

	<u>Money Supply (private sector)</u>		<u>Factors Explaining Increase in Money Supply</u>		
	<u>mil. NCr\$</u>	<u>% Change</u>	<u>million NCr\$</u>	<u>percent</u>	
December 1965	7,891	77.0	Change in Money Supply	5,760	100.0
December 1966	8,801	11.5	Int'l. Reserves	1,810	31.4
December 1967	12,735	44.7	Public Sector Accounts	-2,455	-42.6
December 1968	17,849	40.2	Private Sector Credit	8,511	147.8
December 1969	23,609	32.3	Net Other Assets	-2,106	-36.5

Balance of Payments in 1969 (million \$):

		<u>Merchandise Exports (fob) in 1969:</u>		
		<u>mil. \$</u>	<u>percent</u>	
Exports (goods & services)	\$2,564	Coffee	849	36.8
Imports "	2,467	Cotton	195	8.5
Resource Gap	-97	Iron Ore	149	6.5
Interest Payments (net)	-182	Sugar	115	5.0
Other Factor Payments (net)	--82	Cocoa	136	5.9
Donations (net)	16	All Other	861	37.4
Current Account Bal.	-151	Total	2,305	100.0

Foreign Direct Invest.	126
M< Loan Disbursement	492
M< Loan Amortization	-286
Net Short-Term Credit	528
Other Transactions	-98
Increase in Official Reserves (+)	611

External Debt on Dec. 31, 1969:
(outstanding and disbursed)

Medium & Long-Term	\$2,786
Financial Credits	1,612
Total	\$4,398

Debt Service Ratio in 1969: 18.3%
(excl. amort. of financial credits)

Official Reserves (Dec. 31, 1969):

Net International Reserves	\$1,032 million
Gross Convertible Reserves	\$969 million

Loans from IBRD at Dec. 31, 1969:

Outstanding & Disbursed	\$198.8 mil.
Undisbursed	284.1 "
Total	\$482.9 "

President has seen

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: September 24, 1970

FROM: Gerald Alter *GA*SUBJECT: Meeting of Mr. McNamara with the Minister of Finance of Brazil, Mr. Antonio Delfim Neto in Copenhagen on September 23, 1970

1. Mr. McNamara met with Minister of Finance Delfim Neto who was accompanied by Messrs. Galveas, Pereira Lira, Kafka and Gomes. Messrs. Knapp and Alter were also present. The Minister mentioned that they were now proceeding with the preparation of the agricultural storage project and that he would appreciate the assistance of the Bank in the process. Mr. McNamara indicated that we would be happy to assist and Mr. Alter said that when the preparatory group had advanced somewhat in its work, we were planning to send someone to assist in the formulation of the project.

2. The Minister then requested that the Bank form a joint financing group for the financing of the steel sector (see my memorandum of September 9). In his presentation he stressed the importance they attached to obtaining the full benefits of international competitive bidding, citing the lessons they have learned from the Marimondo project and the experience that they have had with negotiated bilateral financing. Mr. McNamara stated that the Bank would be prepared to help organize joint financing of the steel sector on three conditions. First, there must be a prospect that the steel industry in Brazil would be fully competitive. Secondly, we must be successful in obtaining participation of all major suppliers, with full international competitive bidding. Thirdly, we must be able to fit it into our total lending program. The Minister was in full agreement that the steel industry in Brazil should be established on a competitive basis and he was confident that with the expansion being planned, it would be a very efficient industry. Mr. Knapp stressed the importance we attach to the rational planning of the whole sector and the Minister pointed out that with the three major plans reaching an efficient size, it would be extremely difficult for a new inefficient plant to be established.

3. The Minister expressed the hope that the financing of the steel sector would be over and above what the Bank would otherwise do in Brazil. Mr. McNamara indicated that he could not regard the steel financing as additive but that he did not wish, at this time, to discuss the overall level of Bank financing in Brazil.

President has seen

4. It was agreed that the Bank would assist in organizing the joint financing of the steel sector; the Brazilian authorities would have preliminary discussions with the Inter-American Development Bank and with some of the major supplying countries, including Japan and the U.S. Mr. McNamara would have a meeting with Felipe Herrera in October and would bring the subject up during the meeting.

5. Mr. McNamara suggested that at some convenient time in the future, he would like to obtain the Minister's views on two questions: (a) the political outlook in Latin America as a whole, taking into account the results of the recent Chilean elections, and (b) the outlook in Brazil, in the light of the Minister's conception of how the Brazilian economy was likely to develop in terms of income distribution, regional balance, etc. The Minister said he would be very happy to have a discussion with Mr. McNamara on these points.

cc: Mr. Knapp
Mr. Fuchs
Mr. Wiese
Mr. Husain

GAlter:pa.