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Fonds: Records of the Office of the President

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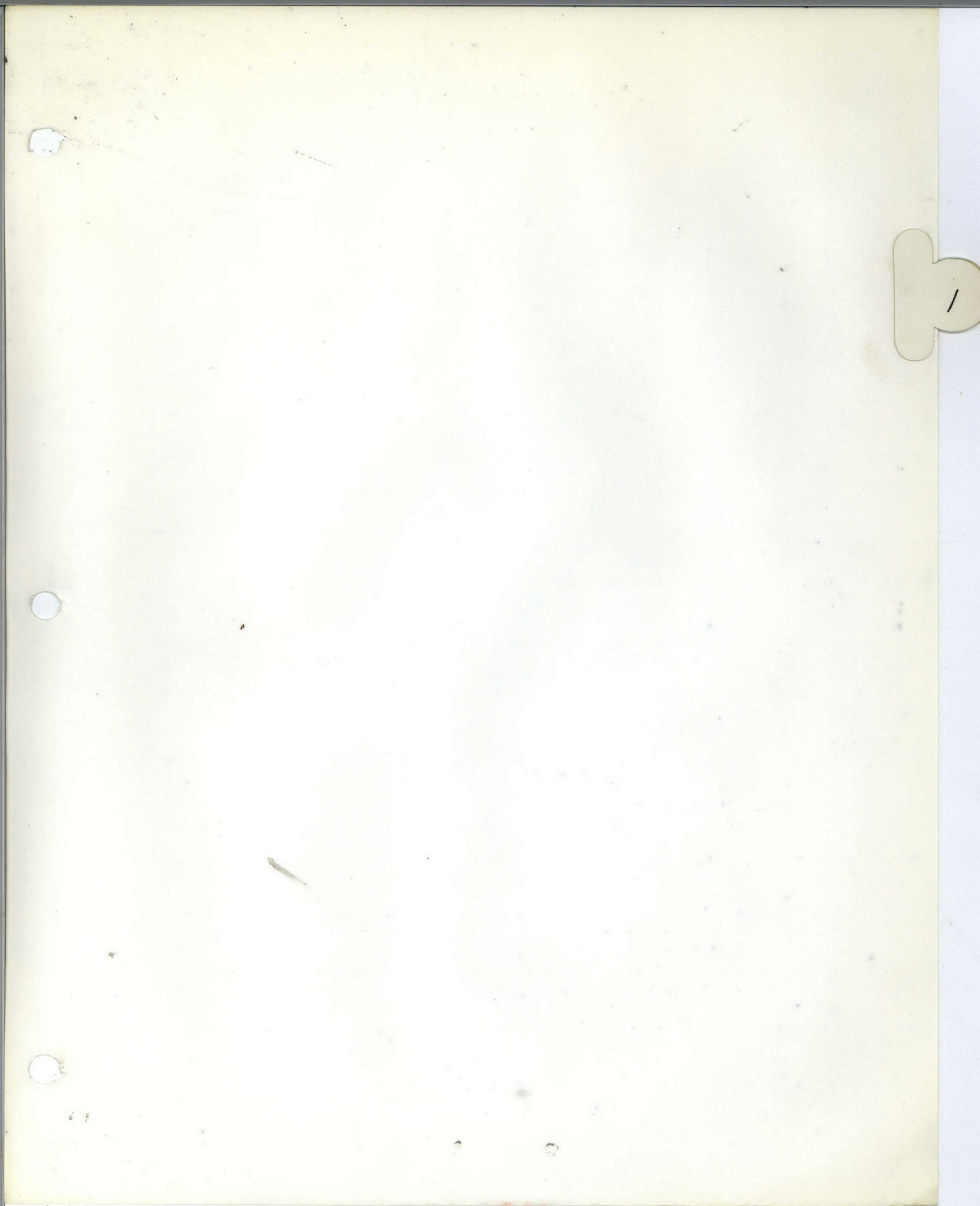
PORTUGAL

PORTUGAL

- 4/9/68 Jose de Mello, Chairman of Banco Totta-Aliance, Lisbon
- 4/26-28/68
(Mont Tremblant
Conference) Alberto F. Nogueira, Minister of Foreign Affairs
1. 10/7/68 Joao Augusto Dias Rosas, Minister of Finance
L.M. Teixeira Pinto, Professor of Economics
Ricardo Faria Blanc, Vice Governor, Banco de Fomento Nacional
Albino Cabral Pessoa, Financial Counselor, Embassy of Portugal
Martim Lencastre Cabral, Assistant for Financial Affairs,
Ministry of Finance
- 5/20-22/70
(Paris) Representatives and Observers at the OECD Meeting:

Valentim Xavier Pintado, Secretary of State for Commerce
Rogerio Martins, Secretary of State for Industry
Joao de Deus Battaglia Ramos, Chief of the Permanent Delegation
Carlos Rogenmoser Lourenco, Vice President of the Technical
Commission of Economic Cooperation
Jose Manuel Sottomayor, Ceputy Chief of the Permanent Delegation
Magalhaes Mota, Chief of Cabinet of the Secretary of State for
Industry
Mme. Maria Angela Vilela, Technical Commission of Economic
Cooperation
Vitor Dias Santos, Cabinet of Planning of the Secretary of
State for Industry
Mario Quartim Graca, Secretary to the Secretary of State
for Commerce
Fernando Moreira de Paiva, Permanent Delegation
2. 3/22/71 Dr. Calvet Magellenes, Director General, Economic Affairs,
Ministry of Foreign Affairs
Martim Cabral, Consultant Advisor to Minister of Finance
Ambassador Vasco Garin
3. 2/24/72 Ambassador Joao Hall Themido
4. 9/19/72 Ambassador Joao Hall Themido
5. 9/28/72 Manuel Cotta Dias, Minister of Finance and Economy
Ambassador Joao Hall Themido
Martim L. Cabral, Adviser to the Minister of Finance
- 6/12/74 Prof. Jacinto Nunes, Acting Gov., Central Bank of Portugal
6. 9/18/74 Mario Soares, Foreign Minister
Ambassador Themido
Mr. Michado, Aide to the Foreign Minister
Albino Cabral Pessoa, Financial Counselor of Embassy

7. 10/1/74 Jose de Silva Lopes, Minister of Finance
Manuel Jacinto Nunes, Governor, Banco de Portugal
Ambassador Themido
Hernani Caeiro Pereira, Vice Governor, Banco de Fomento
Albino Cabral Pessoa, Financial Counselor, Embassy of Portugal
8. 3/17/76 Francisco Salgado Zenha, Minister of Finance
Jose da Silva Lopes, Governor of the Central Bank
Dr. Victor Constancio, Secretary of State for Plan and Budget
Raul Capela, Economic Adviser to the Minister of Finance
Ambassador Themido
Albino Cabral Pessoa, Financial Counselor of the Embassy
9. 12/16/76 Ambassador Themido
Dr. Henrique Carlos Medina Carreira, Minister of Finance
Dr. Jose da Silva Lopes, Governor, Central Bank
Albino Cabral Pessoa, Financial Counselor of Embassy
- 4/20/77 Ambassador Joao Hall Themido, host at dinner for
Prime Minister Mario Soares
10. 4/21/77 Prime Minister Mario Soares
Ambassador Joao Hall Themido
Dr. Medeiros Ferreira, Minister of Foreign Affairs
Dr. da Silva Lopes, Governor of the Central Bank
Dr. Riberio Constancio, Vice Governor of the Central Bank
Mr. Cabral Pessoa, Financial Counselor at the Embassy
- 4/16/81 Mr. Labisa, former Alt. ED



Mr. McNamara - to see please
RHS 10/17

OFFICE MEMORANDUM

TO: Files

FROM: Norman Horsley *X*

SUBJECT: Mr. McNamara's Meeting with the Portuguese
Delegation to the Annual Meeting

DATE: October 14, 1968

Members of the Portuguese Delegation to the Annual Meeting met with Mr. McNamara in his office at the Bank on October 7, 1968. Representing Portugal were:

- Sr. Joao Augusto Dias Rosas, Minister of Finance (Governor)
- Sr. L. M. Teixeira Pinto, Professor of Economics (Alternate Governor)
- Sr. Ricardo Faria Blanc, Vice Governor, Banco de Fomento Nacional (Temporary Alternate Governor)
- Sr. Albino Cabral Pessoa, Financial Counselor, Embassy of Portugal (Adviser)
- Sr. Martim Lencastre Cabral, Assistant for Financial Affairs, Ministry of Finance (Adviser)

Messrs. Knapp and Horsley attended the meeting.

The Minister regretted that recent events in Portugal had prevented him from staying longer in Washington, to which he had come specifically to meet Mr. McNamara. His Government had noted with great pleasure the Bank's policy on economic development since Mr. McNamara assumed the presidency.

The main purpose of the delegation's visit was to confirm the discussion which had taken place in Portugal with the Bank's economic mission and to confirm the Government's agreement with the conclusions of the mission's report. The Minister said that the Government's economic policy was in line with the recommendations of the mission. Specifically it accepted the conclusion of the report that relations between the Bank and Portugal should center on agriculture, and it also accepted the procedure recommended for bringing this about.

Mr. McNamara replied that he was very pleased the Bank's recommendations on agriculture had been accepted, particularly since we had understood that there were differences of opinion between Ministers on this matter. He said that there were two points underlying our relations with Portugal. First, the United Nations attitude which had been expressed in resolutions of the General Assembly: the Bank believed that its Articles of Agreement did not permit it to take political considerations into account, and consequently we could not base our lending policy on the United Nations resolutions. Second, the serious economic problems of Portugal: the Bank appreciated that the new Government had not had time

to come to grips with these problems, and we had understood that there were differences between Ministers as to what policies should be followed, as for example, in agriculture. In particular, Mr. McNamara said that the rate of saving needed to be increased if Portugal were to do what could be done, and policies for industrial growth needed to be changed to permit efficient growth rather than to protect the inefficient. Mr. McNamara said that these and other matters would be discussed in detail in the months ahead; he had mentioned them to demonstrate that our lending policy in Portugal would be based on economic rather than political considerations.

The Minister said that he had noted Mr. McNamara's remarks with great interest and pleasure. He stressed that he was representing the Portuguese Government and expressing agreed policies, showing that the differences with regard to policy mentioned by Mr. McNamara had now been overcome although there might still be some details of policy to be settled or adjusted. He expressed great satisfaction that the Bank took the view it did with regard to the United Nations resolution. Regarding the economic situation, his Government recognized that there were some points where the views of the technical staff of the Bank would have to be taken into account, and this would be done in the months ahead. The Minister asked how we could best get relations between the Bank and Portugal moving. Mr. Knapp said that the most important area for action was agriculture. A mission would be necessary to recommend what should be done, and the Bank would respond favorably to a request from the Government for such a mission. He mentioned the problem of securing FAO collaboration in this instance, but said that this would not prevent us from working out a program.

The Minister asked if it were necessary to include in his Government's request for assistance in agriculture, a specific request for the mission. Mr. McNamara replied that a definite request for a mission was necessary in the light of the difference of opinion between Ministers; he added that he would not send such a mission without a request from the Government. The Minister affirmed that his Government would request both financial and technical assistance from the Bank and would specifically ask for a mission, but would leave the request sufficiently vague for the Bank to determine what type of mission to send.

cc. Messrs. Cope, Fontein, Karasz,
van der Mel, Steckhan,
Balassa, Evans and
Miss Wahl

NH:es

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OFFICE MEMORANDUM

TO: MEMORANDUM FOR THE RECORD

DATE: April 1, 1971

FROM: Jack L. Upper *JLU*SUBJECT: Portugal -- Meeting of Portuguese Officials with Mr. McNamara

Mr. McNamara held a meeting in his office on Monday afternoon, March 22, with Portuguese Ambassador to the United States Vasco Garin; Ambassador Calvet Magelhaes, Director-General of Economic Affairs in the Portuguese Ministry of Foreign Affairs; and Mr. Martim Cabral, Consultant Advisor to the Portuguese Minister of Finance. Messrs. Benjenk, Moro and Upper attended from the Bank.

After explaining that Ambassador Calvet was visiting Washington for discussions with the US Government about the financing of a number of projects, Ambassador Garin said that Portugal was hoping also to find financial support from the Bank. In this respect he was specifically interested in obtaining Bank assistance in the field of education. An ambitious program of educational reform had been announced by the Government, which would, among other things, extend the period of compulsory education from 6 to 8 years. This would require very large amounts of funds to implement, particularly since present facilities were inadequate to provide for 6 years' education throughout the country.

Mr. McNamara responded by saying that the Bank had great interest in education and had developed considerable experience in education projects throughout the world. The demands upon the Bank's experts in this field were very great, and he expressed uncertainty about how soon they might be assigned to assist Portugal in preparing an education project. However, it was noted that an Economic Mission was at present in Portugal, and it was agreed that the mission would be looking into developments in education to some degree. An evaluation of the possibilities for the Bank to become involved in this, as in other sectors, could be made better after their general study on the economy has been completed.

Mr. McNamara outlined the Bank's policy of assisting its more developed borrowers, by helping them to carry out basic structural reforms in conjunction with its lending. He specifically referred to the Bank's experience in Spain, particularly in the fields of education and livestock, where the Bank had supported the Government in undertaking reforms which they wished to make, but which were very difficult to carry out nevertheless, because they were painful for certain segments of the country. He spoke of the many months of preparation, discussion and negotiations which had preceded the financing of both projects.

President has seen

With regard to lending to Portugal, Mr. McNamara strongly disavowed any ideological orientation (citing a number of countries of varying political persuasion, such as Algeria and Congo Kinshasa, where the Bank had recently begun improving relationships). However, he stressed the importance of reviewing economic and social reforms when coming to a judgment about lending to any country and also that the Bank's projects should help a broad section of the population and not just a few, and should encourage a better distribution of income. Mr. Benjenk said that in this respect perhaps a livestock project could include a component for development in the northern part of the country where landholdings were relatively small.

Ambassador Vasco Garin invited Mr. McNamara to visit Portugal in conjunction with his forthcoming trip to Spain. Mr. McNamara regretted that this would not be possible at this time, but hoped to visit the country at some later date.

Cl. with and cc: Mr. Benjenk

cc: Mr. McNamara's office (original + 1 copy)
Mr. Knapp
Mr. Chadenet
Mr. Ballantine
Mr. Evans
Mr. Hartwich

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: March 22, 1971

FROM: M. P. Benjen *DH for:*

SUBJECT: Portugal: Your Meeting with Dr. Calvet Magellenes

Dr. Calvet Magellenes is Director-General of Economic Affairs* in the Portuguese Ministry of Foreign Affairs. He is in the United States to discuss the prospects of US aid to Portugal over the next 5-6 years and will be seeking to know what the Bank can provide within this framework. Dr. Magellenes is accompanied by the Consultant Advisor to the Minister of Finance, Sr. Martin Cabral, who has been active for several years in promoting contacts between the Government and the Bank.

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57 30*

Sr. Cabral explained to Mr. Upper that the program which Dr. Calvet has been discussing with the US State Department and various US Government agencies includes a "shopping list" of projects extracted from the Third Development Plan, 1968-73, estimated to cost over \$400 million in total. The following sectors are included:

'74 Length 15

- Education
- Transport (railways, ports and Tagus Bridge)
- Agriculture (irrigation)
- Industry
- Health (hospitals).

The position that Sr. Cabral takes is that Portugal's own official financial resources are inadequate to carry out this program without external assistance. He feels that the extraordinarily high official monetary reserves, together with a virtually unblemished debt service record, should provide a strong base for more or less conventional external borrowing. There is, however, no intention on the part of the Government to use these reserves for development. Assistance is being sought particularly in those areas which would introduce new technology and "know-how".

The argument for US official assistance runs along the lines that the rights for the US military bases in the Azores were given freely and without request for compensation, but now that the old concepts of self-sufficiency are being changed in Portugal, the need for outside help is becoming apparent. The Government is also anxious to have assistance from the Bank. Officials tend to be outspokenly impatient with the interruption of operations since 1966 and the delay in undertaking an agricultural project since the 1969 Agricultural Survey Mission.

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regulates in their economy
short term of interest
stimulate growth
foundly technical goods? growth
needed by preparing length long
presenting us for approval*

* With rank of Ambassador.

*Highly dependent
in the meantime our
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just not would be properly set*

March 22, 1971

Economic Mission

The Bank's last Economic Mission to Portugal was in early 1968 in the last days of the Salazar regime. Its recommendations were influential in laying the groundwork for the reforms which have been formulated during the past 2-3 years, and the Bank's Agricultural Survey Mission in 1969 was an outgrowth of that report. The Bank's current Economic Mission began work in Portugal only last week, and it will be about three months before we have their assessment of the economic position and prospects.

Livestock Project Preparation Mission

The only operation that we have at present in prospect in Portugal is a livestock project. The project preparation mission returned to Washington at the end of last week after laying the groundwork for project preparation at the working level and discussing their conclusions with the Minister of Finance and the Secretary of Agriculture. The next steps are up to the Portuguese, who have set up a working party to prepare the project. It is expected that this will take 4-6 months, during which another Bank mission could visit Portugal to advise on its preparation. If all goes well, appraisal could take place in early autumn and a loan might be made late in FY 1972. It is likely that the project would be located primarily in the South (Alenteja) of Portugal, where the prospects for livestock improvement are greatest, and conditions are similar to those in Spain. The Livestock Mission concluded that the basic reforms proposed by the Agricultural Survey Mission should be carried out in conjunction with a loan for a livestock project. These include:

- a. increased taxation to induce the productive use of lands now idle
- b. a reduction in the uneconomically high wheat support price, which diverts land use away from livestock with a consequential adverse ecological effect upon the land through erosion and loss of fertility
- c. credit terms at commercial rates of interest and repayment periods in place of the present subsidized rates (3-4 percent interest; up to 20 years' repayment).

General Reforms

Some observations about the present situation with respect to on-going and forthcoming reforms are contained in Mr. Upper's Back-to-office Report, attached.

Attachment

OFFICE MEMORANDUM

TO: Mr. M. P. Benjenk

DATE: March 22, 1971

FROM: Jack L. Upper

SUBJECT: Portugal: Back-to-office Report

My introductory visit to Portugal lasted as scheduled from March 10-17, 1971 and coincided with the final days of the Livestock Project Preparation mission and the first days of the Economic Mission. Mr. Riedl, Loan Officer, joined me March 10-14 and accompanied the Livestock mission to the Northwestern region.

During my visit I had the opportunity for general discussions with a number of officials and bankers, in and out of government. I also attended meetings with the Livestock and Economic Missions, who will be submitting separate back-to-office reports.

Any assessment of the general situation in Portugal at the present time, and in particular of the kind of reforms which are taking place and the probability of their success, must take into account the delicate and cautious balance which is maintained between the small but growing group of reform-oriented, open-minded and relatively young officials whom one meets most frequently in the economic secretariats and the powerful representatives of the old traditional establishment who remain in strong positions both in the government and throughout the economy. It is recognized by most officials that achievement of effective change over the longer-term therefore requires prudent action to avoid a reversion of social and political life into the patterns of the recent past. It is in this context that political continuity is constantly referred to as one of the virtues of Portuguese society. This generally implies the preservation of a paternalistic relationship with the overseas provinces and the absence of political parties. Even these formerly unquestioned assumptions are coming under challenge to some extent, as evidenced by the proposed constitutional revisions before the Parliament which would grant a degree of autonomy to the overseas provinces and the recent formation of a quasi-political group aiming at social and economic change. Several of the young technocrats in government have a leading role in this group. Some freedom has also recently been granted to the trade unions to choose their own leaders without government approval. The speeches of the reformist members of Parliament, which were withheld from the press last year, are now being reported regularly, and are usually accompanied by commentary.

The outcome of the reform discussions which have been going on in the government for the past 2-3 years is now before the Parliament in the form of a series of legislative proposals.

March 22, 1971

Constitutional revisions which would, inter alia, give a degree of autonomy to the overseas provinces have been under review by Parliamentary Committee and are expected to be reported out momentarily for consideration by the full Parliament. A special session has been scheduled in May for this purpose. The persons with whom I discussed this question felt that the legislation would be adopted without much change. Speculation as to its effect ranged widely, even going so far as raising the possibility of eventual UN membership. In any case, indications were that a real change is in the offing.

Far-reaching reforms were announced by the Minister of Education in January 1971, some of which are already in effect, and others are under consideration by Parliament. Free and open admission to the universities has already caused many difficulties due to shortage of space and faculty, and student disturbances appear to be widespread. The proposed extension of compulsory primary education from 6 to 8 years and the building of vocational schools will require major investments and restructuring of the educational system, which is still in the early planning stages.

The difficult choices lying ahead as association with the European Economic Community is established were on the minds of several officials. It is expected that the type of agreement to be negotiated will be apparent by the end of the year, but in the meantime considerable uncertainty prevails. This in itself creates a climate receptive to change. A draft industrial law introducing a number of reforms, including the gradual elimination of protective industrial licensing restrictions, was submitted to Parliament on March 15. Active consideration is not expected until after the constitutional revisions have been passed and perhaps only after the 1972 budget has been reviewed in October, but very high priority is being given to it. A basic restructuring of industry is envisaged whereby powerful incentives would be given to new industries and to the reorganization and merger of existing companies (many of which are family owned), a special body for industrial promotion (government loans, grants, guarantees, exemptions, etc.) and overseas investment centers would be set up. Licensing of production facilities would be limited to basic industries such as steel and oil refining.

One gets mixed, and often conflicting, impressions during a short visit to Portugal. The word "transitional" is often used to describe the present state of affairs. The way ahead is far from clear, but the stage is clearly being set for constructive change. It appears that the Bank can have a useful role through projects which initiate, accelerate and intensify structural changes.

Livestock Project

A livestock project would provide a good potential for the Bank to play just such a role. The types of reform that are needed

Mr. Benjenk

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March 22, 1971

are discussed in the Agricultural Survey Report. Particularly important are taxation on land to induce its productive use, a reduction in the wheat support price and commercial terms for agricultural credit.

Together with Messrs. van Gigch and Clarke, I met the Minister of Finance and the Secretary of Agriculture to discuss the findings of their mission. Both officials acknowledged that reforms were needed for livestock development. The Minister of Finance was skeptical about obtaining these quickly, but at the same time he was very impatient to have quick action by the Bank on the project and seemed prepared to accept the conditions necessary to achieve that. The Secretary of Agriculture gave much emphasis to social aspects of agricultural development and seemed receptive to the types of change needed. He was particularly interested in cooperative programs in the North and may press for the inclusion of such a component in the project.

cc: Mr. Hartwich
Mr. Thompson

February 25, 1972

MEMORANDUM FOR RECORD

SUBJECT: Visit of Ambassador Hall Themido of Portugal, February 24, 1972

The Ambassador mentioned that he had presented his credentials recently and that he had met Mr. McNamara formerly at NATO meetings. He regretted that Bank/Portugal relations were not as good as he would wish.

Mr. McNamara said that he had spoken to the Foreign Minister on this subject and said that previous decisions not to lend to Portugal as well as the Bank's present position were entirely based on economic considerations. The Bank will not make decisions on political grounds and at present economic environment in Portugal does not warrant a change of position when 40% of the budget and 7% of GNP are spent on defense.

The Ambassador mentioned similar cases of India and Israel and Mr. McNamara replied that in India the figures are not of that order and that Israel which does spend much on defense faces special threats but is a marginal case for Bank lending.

The Ambassador volunteered to provide figures and information showing that Portugal does also face outside threats in its territories in Africa and that, although defense expenditure is high, part of it in fact goes to development in the form of infrastructure. Angola and Mozambique are presently experiencing an economic boom and the people are loyal to the Portuguese Government. In addition, Portugal is receiving no outside military assistance. He appealed to Mr. McNamara to help improve Bank/Portuguese relations.

Mr. McNamara agreed that many developing countries are spending too much on defense. However, the Bank does have its economic standards to which it must adhere. He proposed that the discussion be kept open and suggested the Ambassador come to lunch when he had something to report or propose.

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February 25, 1972

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OFFICE MEMORANDUM

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WBG ARCHIVES

TO: Mr. Robert S. McNamara
FROM: Dieter Hartwich *HH*
SUBJECT: Visit of Dr. Joao Hall Themido, Ambassador of Portugal to the United States on Thursday, February 24

DATE: February 22, 1972

Biographical background

4/2/03

Joao Hall THEMIDO presented his credentials as Ambassador of Portugal to the United States on December 6, 1971. He had formerly served as Portugal's Ambassador to Italy (and concurrently to Malta) from February 1968 until November 1971, when he arrived in Washington.

Dr. Themido was born in Coimbra, Portugal on January 6, 1924. He is a graduate of the Law School of Coimbra University and a career diplomat. He has held posts in: Tangier (1948-50); New Delhi (1950-52); London (1958-60); and was Assistant Director General and Director General for Political Affairs in the Foreign Ministry, Lisbon (1961-68). He has served as an alternate delegate to the UN General Assembly, 17th Session (1962), and as representative to a NATO Ministerial meeting (May 1965).

Dr. Themido speaks English, Spanish and French in addition to Portuguese. He is married to the former Lydia Falcao de Freitas. They have no children.

Probable purpose of his visit

Dr. Themido, in addition to making a protocol call on you, will probably raise the question of Bank lending to Portugal, particularly in the agricultural sector. I understand that the Foreign Minister asked U.S. Secretary of State Rogers at the time of the last UN General Assembly to intervene with the Bank to look more favorably on lending for agriculture, as well as for education, for which new and comprehensive plans have been made. The State Department suggested that Portugal present its case directly to the Bank.

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OFFICE MEMORANDUM

TO: MEMORANDUM FOR THE RECORD

FROM: M.P. Benjenk 

SUBJECT: PORTUGAL : Visit of Ambassador Themido with Mr. McNamara

DATE: September 21 1972

The Ambassador of Portugal, H.E. Joao Themido, called on Mr. McNamara on Tuesday, September 19. The purpose of his visit was to inform Mr. McNamara of the wish of the new Portuguese Minister of Finance, Mr. Cotta Dias to meet with Mr. McNamara and discuss the relations between Portugal and the Bank, which were not altogether satisfactory. The Minister of Finance had a preference for seeing Mr. McNamara during the Annual Meeting but realized that this was a busy time and was therefore quite prepared to make a separate trip to Washington at a later date to see Mr. McNamara.


Mr. McNamara replied that he would not wish the Minister to inconvenience himself by making a separate trip and he would be glad to see him during the Annual Meeting (appointment was thereafter made for Friday, September 29 at 3 p.m.).

The Ambassador warmly thanked Mr. McNamara on behalf of the Minister of Finance.

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: September 15 1972

FROM: M.P. Benjenk SUBJECT: Portugal - The Ambassador's Visit

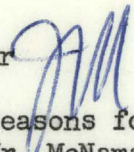
Please find attached a memorandum from Mr. Upper, the Division Chief responsible for Portugal, concerning the presumed purposes of the Ambassador's visit to you on Tuesday, September 19. I also attach an intra-departmental briefing paper on Portugal.

9/18
Att:

OFFICE MEMORANDUM

TO: Files

DATE: September 15, 1972

FROM: Jack L. Upper CONFIDENTIALSUBJECT: Portugal: Reasons for Ambassador's Visit to
Mr. McNamara on September 19

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As Mr. Benjenk requested, I spoke yesterday afternoon to Mr. Pessoa, Financial Counsellor at the Portuguese Embassy, to inquire the purpose of his Ambassador's proposed visit to Mr. McNamara on Tuesday, September 19 (scheduled at 11:15 a.m.).

Mr. Pessoa said that his Ambassador had met the new Minister of Finance and Economy recently in Lisbon and that the Minister felt that it would probably be neither propitious nor convenient for Mr. McNamara to see him during the busy Annual Meeting but that he would like to have the opportunity to meet with him on a later trip which he would schedule at Mr. McNamara's convenience. The purpose would be to follow up the Ambassador's conversations with Mr. McNamara earlier this year when the Ambassador explained that Portugal's defense expenditures include a number of items which might equally be classified as infrastructure in other countries and that there are no hidden elements in the defense budget in the form of gifts from other countries, etc.

The new Minister of Finance and Economy Dr. Manuel Cotta Dias assumed office in early August 1972 when Mr. João Augusto Dias Rosas returned to private life after five years as Minister. He is 43 years old, a lawyer by profession, and is also President of the Executive Committee of National Popular Action (ANP), Portugal's dominant political party. Cotta Dias also served as Premier Caetano's secretary when the latter was rector of Lisbon University. He was most recently Vice Governor of the Banco de Fomento Nacional and Chairman of the Commission for Economic Coordination in Portugal.

The Ministry of Finance and Economy encompasses secretariats of industry, agriculture and commerce, which are frequently separate ministries in other countries. The secretaries of these sub-ministries have changed along with the Minister. These officials, together with the Planning Chief, had represented the liberal and pro-European wing of the Caetano Government. In particular, the Secretary of Commerce (Pintado) had worked toward a liberalization in foreign trade and an agreement with the EEC, and the Secretary of Industry (Martins), the author of the May 1971 Industry Laws, had tried to strengthen the competitive forces within the Portuguese economy. With their departure, the Government appears to be shifting back to its earlier more conservative position with less emphasis on developing relations within Europe and greater concentration on maintaining control over Portugal's overseas provinces.

President has seen

Files

- 2 -

September 14, 1972

It has been reported to the State Department that, in spite of their relatively conservative orientation, the new Minister and his Secretaries are very interested in establishing good relations with the Bank.

A copy of the Annual Meeting brief is attached.

cc: Mr. Benjenk

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WBG ARCHIVES

CONFIDENTIAL

September 13, 1972

1972 BRIEFING PAPER - PORTUGAL

(For possible departmental meeting)

I. MEMBERS OF DELEGATION

Dr. Manuel <u>Cotta Dias</u> (B)	Minister of Finance and Economy
Professor Daniel Maria <u>Vieira Barbosa</u> (B)	Governor of Banco de Fomento Nacional
Antonio Manuel <u>Pinto Barbosa</u> (F)	Governor, Banco de Portugal
Manuel Jacinto <u>Nunes</u> (F)	Vice Governor, Banco de Portugal

ADVISERS

Martim <u>Cabral</u> (B)	Assistant to Minister of Finance
Alvaro <u>Ramos Pereira</u> (F)	Director, Banco de Portugal
Carlos <u>Saldanha de Valle</u> (F)	Technical Advisor, Banco de Portugal
Dr. Luis <u>Gois Figueira</u> (B)	Counsellor of Embassy, Ministry of Foreign Affairs
Dr. Albino <u>Cabral Pessoa</u> (B)	Financial Advisor, Portuguese Embassy

II. GENERAL

During the last year relations between the Bank and Portugal have been dormant if not moribund. Prior to the 1971 Annual Meeting the Portuguese Embassy was informed that while there were promising features in recent economic developments in Portugal, the management of the Bank felt that the performance still did not justify a resumption of Bank lending. The Portuguese were told that the most disturbing feature in the economic picture was the very high proportion

of the budget and of GDP devoted to military expenditures, and that since Portugal was one of the more prosperous developing countries, Bank lending to it could only be justified if it devoted all its energies to economic development.

The Portuguese were greatly disappointed by this position and the Finance Minister met neither with Mr. McNamara nor Mr. Benjenk during the meeting. In an informal meeting the Advisor to the Ministry of Finance said they thought Portuguese economic performance had improved considerably within the last three years and they had expected that a Bank loan in the agricultural sector might eventually be made following the economic and agricultural studies undertaken by the Bank during recent years. The Portuguese officials also hoped that some way might be found for a continuing relationship with the Bank, such as technical assistance or some form of assistance to the Overseas Territories. The Portuguese also felt that Portugal was being discriminated against compared to other countries with relatively high income levels and high levels of defense expenditures, such as Israel, Greece and various Middle Eastern countries.

For its part, the Bank has made available Mr. Bela Balassa as a consultant on questions of industrial policy and protection. On two visits to Portugal Mr. Balassa reviewed work done by the Secretariat of Industry, and had discussions with the Governor of the Bank of Portugal, some government officials and several private industrialists on questions relating to Portugal's association with the European Common Market. In carrying out work on the system of protection in Portugal, the Secretary of State for Industry has utilized methodology developed at the Bank. The study is now to be updated to 1970 and various modifications agreed on between Mr. Balassa and the Secretariat will be made in the work done so far.

Mr. Balassa also prepared a report for the Government on "The implications of Portugal's Association with the European Common Market". It considers the problems facing Portugal in a free trade area in industrial goods with the EEC, and contains suggestions for improving the competitiveness of Portuguese industry.

III. ISSUES TO BE RAISED BY THE BANK

A. Appreciation might be expressed for Portugal's subscription of \$1 million to the Bank's September 1972 bond issue. Their holdings now total \$4 million. ✓

B. Mr. Balassa's report might be mentioned and the representatives be sounded out on the status and implications of Portugal's trade agreement with the EEC. ✓

IV. ISSUES TO BE RAISED BY PORTUGAL

A. The delegation may question whether the Bank's position on lending to Portugal remains the same as last year. In reply the delegation might be asked about the continuing large share of defense expenditures in the budget and the portion of annual public expenditures devoted to economic development. The following table compares military expenditures as percentages of GNP in several countries in the area. These do not include internal security or foreign grants and credits available for defense expenditures only. However, although these data have limitations for the purpose of internal comparison, they still indicate a general relationship.

	<u>Defense Expenditure as % of GNP in 1971</u>
Portugal	7 *
Israel	26
Egypt	14
Greece	3-4
Jordan	14
Iraq	13
Iran	10
Nigeria	7
Syria	8

* Ratio to GDP for 1970

5

DECLASSIFIED

MAY 09 2013

WBG ARCHIVES

CONFIDENTIAL

October 5, 1972

MEMORANDUM FOR THE RECORD

PORTUGAL: Meeting of Minister of Finance Cotta Dias With
Mr. McNamara During the Annual Meeting

Mr. McNamara met with the Portuguese delegation consisting of the newly appointed Minister of Finance Cotta Dias, the Ambassador to the United States Dr. Themido, and Mr. Martim Cabral, Adviser to the Minister of Finance. Mr. Benjenk and Mr. Upper attended. Mr. Cabral translated.

16/6
The Minister said that, following a change in Cabinet in August, he was pleased to greet Mr. McNamara as the new Governor for Portugal. He would also be delighted if a new phase in relations with the Bank could begin. He felt that the Fourth Development Plan now being prepared in Portugal to begin in 1974 could provide a good opportunity for such cooperation and that its main objectives would be fully consonant with Mr. McNamara's speech at the Annual Meeting.

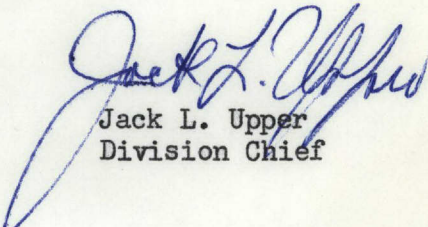
Mr. McNamara said that the Bank was restricted in its lending to Portugal for two reasons: (a) income per capita was higher than in the majority of Bank member countries, and (b) the level of defense expenditures both as percent of total government expenditures and as a percent of GNP was high. This latter factor could lead member governments to argue that Portugal was not using her resources as effectively as possible and that the Bank was therefore not justified in making loans. In sum, the possibilities of the Bank helping finance the Fourth Plan were not great, but, on the other hand, not entirely ruled out. Other forms of relations were possible; the Bank could consider the needs and possibly provide assistance, as in the case of Professor Balassa.

Minister Cotta Dias replied that Portugal was interested in all types of assistance, including technical assistance, but that he hoped to move towards Bank financing. He felt that the Bank should look more carefully into the nature of defense expenditures and the budgetary headings under which they appeared, some of which he felt were not actual defense categories. Mr. McNamara said that defense expenditures were particularly difficult to examine, because they are frequently confidential, but he would be willing to discuss individual categories if the Government so wishes.

President has seen

Mr. McNamara also mentioned the difficult problem of UN relations. He pointed out that both he and his predecessor had taken the position that the Bank under its articles would not take into account political considerations, and he was therefore unwilling to accept the limitations imposed by various UN resolutions. He noted that there had been much criticism of the Bank's stand, particularly in the Economic and Social Council. Nonetheless he would continue to maintain his position vis-à-vis the UN. Still the level of defense expenditures in Portugal affected economic performance too much to justify lending. Perhaps if over time measures to promote social advances are taken, the Bank could help in various ways. As a first step, in any case, we should work on technical assistance.

The Minister expressed his understanding of the situation and suggested that the Ambassador would always provide a quick channel of communication if needed.


Jack L. Upper
Division Chief

Cl. with and cc: Mr. Benjenk

cc: Mr. McNamara (2)
Mr. Knapp
Mr. Votaw

Europe, Middle East and North Africa Region
Division 1D

6.

MEMORANDUM FOR THE RECORD

Meeting with Minister of Foreign Affairs Soares of Portugal, September 18, 1974

Present: Messrs. McNamara, Soares, Michado (the Minister's Aide), Ambassador Themido and Counsellor Pessoa, and Benjenk

Mr. McNamara congratulated Minister Soares to his accomplishment in foreign policy.

Minister Soares said he wanted to outline where Portugal was going. The country had changed profoundly including relations with its colonies. Guinea-Bissau had been set free a few days ago. Mozambique would acquire independence on June 25, 1975 and they were addressing the problem of Angola. Profound reconstruction and readjustment is necessary in Portugal after 48 years of dictatorship. This would be a complex process since radicalization of the left is unavoidable after dictatorship. This was noticeable already in the army, the press and the church. The Government wished to stabilize a democratic system.

These were the reasons for Minister Soares to visit the U.S., the EEC and the Bank, since Portugal would need help in its economic program. He was aware that the World Bank had been closed to Portugal, presumably due to its colonial policies and UN resolutions denouncing them. He hoped for a new understanding from the Bank and emphasized his worry about sliding too far down to the left. Spain would see radical changes soon and Greece had been in great turmoil. He said the U.S. Government has reason to worry on international political grounds.

Mr. McNamara said that Minister Soares was right that the Bank had not lent to Portugal since 1966. The reason, however, was not the UN resolutions or colonial policies since the Bank's Articles prohibit lending programs to be influenced by political factors. The sole criterion must be whether economic program is sound and beneficial to the majority of the people of the nation. This had not been true. The military effort in Africa had been a serious misallocation of resources. He now understood that this would be changed and, if policies are sound, the Bank would be pleased to help. He suggested that Mr. Benjenk visit Portugal on an exploratory mission to discuss Portugal's economic plans.

The Minister welcomed this suggestion and invited Mr. Benjenk to meet with anyone who may help the Bank in understanding the situation. He said the Government is provisional with elections scheduled for March 1975. The Government does not intend to change the economy or society profoundly except for some basic changes towards democratization, but short-term economic plans do exist.

Mr. McNamara said that he was embarrassed that the Bank knows so little about Portugal, perhaps less than of any other of the 100 countries where it operates. He said that the Bank would be pleased to discuss the details of cooperation with the Minister of Finance during the Annual Meeting. Minister Soares was in full agreement.

Mr. McNamara repeated his congratulations for Minister Soares' personal accomplishments in the interests of Portugal and the world.

AL
September 19, 1974

OFFICE MEMORANDUM

DECLASSIFIED


MAY 09 2013

WBG ARCHIVES

DATE: September 18 1974

CONFIDENTIAL

TO: Mr. Robert S. McNamara

FROM: M.P. Benjenk 

SUBJECT: PORTUGAL: Visit of the Foreign Minister

9/18

The Foreign Minister of Portugal, Mr. Mario Soares, will visit you this evening. Mr. Soares is in his mid-forties and a lawyer by training. He is also the head of Portugal's Socialist Party and one of the most influential figures in the present cabinet. He has been the architect of the semi-secret negotiations which have led to the recognition of the independence of Guinea-Bissau and the recently announced agreement between Portugal and the Frelimo, the revolutionary movement in Mozambique. In his negotiations Mr. Soares had used the good offices of both Algeria and the Organization of African Unity. There still remains the problem of Angola to be resolved -- it might be interesting to find out what the prospects for independence of that last Portuguese colony are.

Mr. Soares, who is on the left of the political spectrum in the present administration, spent many years in exile in Paris before he was recalled to Portugal by General Spínola, author of this Spring's coup against the former regime. Mr. Soares is leading his country's delegation to the General Assembly meeting of the United Nations.

Relations with the Bank

I am attaching a briefing paper intended for your meeting with the Minister of Finance during the Annual Meeting. As you know we have not lent to Portugal since 1966 and our last economic mission went to Portugal in 1971. We now have to decide whether we should resume active relations with Portugal. In the light of the performance of the new government so far, my answer would be positive. While Portugal does not face any immediate balance of payments crisis -- it has ample reserves -- and has not yet drawn on the IMF, the need for structural reforms in practically every sector is obvious and is equally true of the machinery of government as concerns planning and public administration. I am sure the Bank would be very helpful at this critical time in Portugal's history.

If you also feel that a resumption of relations is now appropriate, I would suggest the way to begin would be to treat Portugal for all practical purposes, as if it were a new member country. When Romania joined the Bank I visited Bucharest, accompanied by the head of the prospective economic mission, to identify the general intentions of the regime and arrange preparation for the economic mission. This was followed by sectoral and project missions which were arranged as a result of the first visit. I would propose to act similarly with regard to Portugal.

Att:

October 10, 1974

Portugal: Annual Meeting 1974
Meeting with Portuguese Delegation

1. Present: Messrs. da Silva Lopes (Minister of Finance), Jacinto Nunes (Governor, Banco de Portugal), Ambassador Themido, Caeiro Pereira (Vice Governor, Banco de Fomento), Cabral Pessoa (Financial Counselor, Embassy), McNamara, Benjenk, Paijmans and Köpp.

Cooperation Between Portugal and the Bank

2. Minister da Silva Lopes expressed the hope that general political acceptance of the new situation in Portugal by the international community would counterbalance the unfavorable effects on Portugal of the present economic situation in the world. Traditionally, Portugal's balance of payments had been positive but recently it had shown a rapidly increasing deficit. The country, the Minister said, needed support, both financial and technical, from IBRD, in order to establish and implement a sound development program and to avoid too drastic a reduction of its reserves.

3. The Minister emphasized that agriculture and small and medium sized industry should have first priority in Bank financing but he mentioned also possible projects in transportation (railways, road improvement), education and fisheries. He made a great plea for reconsidering a livestock project which had been proposed for financing already several years ago when the Bank was considering (but decided against) a resumption of lending to Portugal. He argued that this project already had been reviewed by the Bank and therefore needed only some updating and that the present Government would be very much in favor of all reform elements which had been proposed by the Bank previously.

4. The Minister also suggested to have a discussion on eventual Bank assistance to Portugal's overseas territories when they became independent, especially Mozambique.

5. Mr. McNamara replied that he felt the Bank knew so little about Portugal. He emphasized that the Bank would have to review the economic situation of the country first before it could proceed with any projects for lending. It would be a disservice to the Government if the Bank gave advice without knowing the situation. The Government should be aware that the Bank would need a lot of information to evaluate the situation and that it would take some time before actual loans could be processed. He mentioned that Mr. Benjenk planned to visit Portugal in November to prepare the ground for an economic mission.

Overseas Territories

6. On possible assistance to Portugal's overseas territories, Mr. McNamara indicated that he would discuss with Messrs. Knapp and Benjenk how to accelerate Mozambique's admission to the Bank and which procedures to establish for this purpose.

Recent Events

7. In response to a question by Mr. McNamara, the Minister briefly commented on the recent political events in Portugal, i.e. the resignation of General Spínola and his succession by General Costa Gomes as President of Portugal. In his view this change in the presidency would not affect the basic political and economic orientation of the new Government. The new and old presidents were friends. The change in the presidency was, in his view, the result of a clash of personalities, not a change of policy. The Government should be viewed as a temporary government until general elections would take place which still are scheduled for March 1975.

Hans-Eberhard Köpp
Division Chief
Country Programs Department I
Europe, Middle East and North Africa Region

Cl. with and cc: Mr. Paijmans

cc: Messrs. McNamara (2), Knapp, Benjenk, Wapenhans, Maiss,
Köpp, Hume, Zaman, Lachman

HEKöpp:orp

8.

OFFICE MEMORANDUM

TO: Memorandum for the Record

DATE: March 18, 1976

FROM: Martijn J.W.M. Paijmans

J
DECLASSIFIEDCONFIDENTIAL

MAY 09 2013

SUBJECT: Visit of Portuguese Delegation

WBG ARCHIVES

1. On March 17, Mr. McNamara received a Portuguese delegation consisting of:

H.E. Francisco Salgado Zenha, Minister of Finance
Mr. Jose da Silva Lopes, Governor of the Central Bank
Dr. Victor Constancio, Secretary of State for Plan and Budget
Mr. Raul Capela, Economic Adviser to the Minister of Finance
H.E. Joao Hall Themido, Ambassador to the U.S.
Mr. Albino Cabral Pessoa, Financial Counselor of the Embassy.

Mr. Rota and I were also present.

2. The Minister explained that the purpose of his visit to Washington was to reinforce relations with the U.S., to which effect he had held discussions with several members of the Government. A further objective of his visit was to meet again with Mr. McNamara and to answer any questions he might have. The Minister explained that Portugal needed the understanding of the Bank for its situation; he frankly felt that we had several doubts in that respect and he was ready to answer any questions. The Minister added that he was convinced of the Bank's friendly attitude vis-a-vis his country.

3. The Minister presented a brief description of the political situation as it evolved after the revolution overthrew "half a century of dictatorship" and he emphasized the efforts of the current Government (which came into power after the unsuccessful attempt for a putsch was defeated in November 1975) to stabilize the situation. He recognized that the economic situation remained difficult, with 350,000 refugees in a new democracy in a poor country.

4. The Secretary of the Plan and Budget briefly presented the economic situation as it is known already to the Bank. New information was that the Government, only a few days ago, had approved new structures to provide external trade credits and had defined conditions for export insurance. Also the statutes of the new public power company would be approved by the end of the current month.

5. In summary, he said that the Government fully realized that investment, production and export had to be stimulated and consumption restrained, and he explained the measures already taken. He mentioned specifically that although confidence from the private sector is rising, it will take some time before private investments are stepped up. In the meantime, public investment will have to play an important role. The Government's objective is reflation through investment and exports, addressing in particular unemployment and idle capacity. He mentioned specifically the serious balance of payments problem and Portugal's need for long-term capital.

March 18, 1976

6. In this respect the World Bank role was important, said Mr. Constancio. Portugal realized they were not always in a position to provide data up to the normal standards of the Bank, and he pleaded indulgence. The Government would like to see faster progress in project financing. The Government would like to receive Bank assistance firstly in:

- i) Transportation infrastructure: Highways, railways (in the latter they also have technical problems on which they would like to have our advice);
- ii) Agriculture: Here they badly need technical assistance for project preparation. Also, the Ministry of Agriculture is inefficient and traditional - this problem needs addressing. Portugal imports 50% of its food requirements - this situation needs to be changed;
- iii) the Portuguese Development Bank;
- iv) also, but less urgently than the above, in Education.

7. In his response, Mr. McNamara explained the Bank's friendly attitude toward Portugal, and its willingness and duty to assist a member country. He recognized Portugal's problems and the strong steps the Government has taken and is taking, in spite of its being in office for barely 90 days. He wanted the Minister to realize that several factors play in our investment process:

- i) Creditworthiness. He was prepared to say that for the power project Portugal was creditworthy; beyond that, and particularly in the medium run, this assessment would depend on how Portugal would progress.
- ii) Satisfactory economic performance. For the moment, considering the short period the Government had been in power, he felt this was satisfactory.
- iii) Satisfactory projects. The power project looked good, negotiations would take place shortly, and he expected the project to go to the Board in late April.
- iv) Bank's resource position. We are limited.

8. Mr. McNamara said that we would "push hard on Power" and "move Roads as rapidly as we can", although the latter could not be in this fiscal year because staff work still needed to be done. Work on other projects would now begin. The Bank would do everything it can, but Mr. McNamara warned that this had to be within the limits of Portugal's creditworthiness and performance as the Bank itself utilizes borrowed funds. He repeated however to be encouraged by the Government's approach to the economic situation which he considered very sound.

March 18, 1976

9. Mr. McNamara also explained the difficulties that normally emerge when a country and the Bank start a (new) lending relationship. These can only be solved if both sides are sympathetic to each other's needs and limits.

10. The Minister expressed his gratitude for Mr. McNamara's reception and words. He had never doubted the goodwill of the Bank toward Portugal and understood the link we have to make with economic performance. He emphasized again the importance of Portugal's struggle and the need for sympathy and understanding.

MPaijmans:gg/sap

cc: Mr. McNamara's office (2)
Mr. Knapp
Mr. Wapenhans
Mr. Wyatt
Mr. de Lusignan

OFFICE MEMORANDUM

TO: Mr. R.S. McNamara, President
THROUGH: Mr. J. Burke Knapp, Senior Vice President, Operations
FROM: Willi A. Wapenhans, Vice President, EMENA

DATE: March 16, 1976

SUBJECT: PORTUGAL: Proposed Five-Year Lending Program

1. Further to our discussion with Mr. Knapp on Monday, March 15, I am attaching a revised lending program for Portugal through 1980.
2. Although specific sectors are identified, most projects are still to be defined, and I should emphasize the very tentative nature of this proposed program beyond FY1977. The early years concentrate on infrastructure (power, roads and rails) and development finance. These conventional operations would help provide urgently required external development capital. They would also assist in important structural reforms and lay the basis for workable relationships with governmental institutions. The latter years, however, move into more difficult sectors (agriculture and education) which will require a considerable amount of preparatory work. The inclusion of these sectors in the proposed program after FY1977 is predicated on the assumption that the Portuguese will give them high priority for future Bank lending.
3. The proposed program has an average annual lending of \$73 million for a total of \$365 million in the five-year (76-80) period. However, because of delays in starting operations, the first two years are considerably below average with the last three years being above average to permit catching up. This results in an annual average per capita lending of \$8.52 in current dollars and \$5.01 in constant 1974 dollars, based on a 1974 population of 8.57 million.

Attachment

cc: Messrs. Paijmans
de Lusignan

PESmith/GdeLusignan:pl

1974 Population : 8.57 million
 (1973) GNP Per Capita : \$1410
 Population Growth Rate: 0.9%
 Exchange Rate : US\$1 = 25.4 escudos (1974)

PORTUGAL: ACTUAL AND PROPOSED PROGRAM OF LENDING OPERATIONS THROUGH FY1980
 (US\$ million)

	Through 1975	Program					Totals 1969-73	Totals 1974-78	Totals 1976-80	Reserve Projects
		FY76	FY77	FY78	FY79	FY80				
Agricultural Credit					35.0*					
Irrigation (unidentified)										
Livestock										
Rural Development					30.0					
Education I				30.0						
Education II									30.0 (80)	
DFC I			30.0							
DFC II				30.0						
Highways I			20.0							
Highways II				35.0						
Railways				30.0*						
Power I - V	57.5									
Power VI		30.0								
Water Supply and Sewerage (unidentified)										
LENDING PROGRAM		30.0	50.0	95.0	95.0	95.0	175.0	365.0		
IBRD Number		1	2	3	3	3	6	12		
Lending Program in Constant FY74 \$ Million		19.9	31.6	57.0	54.4	51.7				
Commitment Deflator		150.4	158.4	166.4	174.7	183.5				
Standby Projects			30.0	35	30.0	-				
IBRD Number			1	1	1					

* Standby

Europe, Middle East and North Africa Region
 March 15, 1976

OFFICE MEMORANDUM

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

DATE: March 11, 1976

FROM: Martijn J.W.M. Paijmans, Acting Vice President, EMENA Region

SUBJECT: PORTUGAL: Visit of the Minister of Finance and the Governor of
the Central Bank.

1. While you were away, the Embassy of Portugal asked your office for a meeting with Minister of Finance Francisco Salgado Zenha, and the Governor of the Central Bank, Jose da Silva Lopes, who will be arriving in Washington next Monday for a series of discussions on March 16, 17 and 18. They will be accompanied by Dr. Victor Constancio, Secretary of State for Plan and Budget and Mr. Raul Capela, the Economic Adviser to the Minister of Finance.

2. During this visit, the Portuguese delegation will meet with United States officials, in particular, with the Secretary of State and representatives of Congressional Committees. In addition, at the IMF, Mr. H. J. Witteveen has arranged for a working lunch on March 17. Since a meeting with you has been requested, I would appreciate it if you could let me know what would be the most suitable time. The delegation is ready to meet you at your convenience and, if necessary, late in the afternoon.

3. The purpose of this visit is, prior to the legislative elections of April 25, to inform the United States Government of the present Portuguese situation and of its prospects. The delegation also wishes to inform you of the problems facing Portugal's economic development and it is expected that they would like to know more about the Bank's intentions regarding financial assistance to their country.

4. As you know, under our current operations, we are processing two loans: one for power, in the amount of \$30 million; and the other for highways, in the amount of \$20 million. The proposed loan for power has been submitted today to the Loan Committee. Our present plans are to present it to the Board on April 29, assuming negotiations begin before the end of this month. The highway project was appraised in December; however, because of additional data requirements, a mission will be in Lisbon during the latter part of this month to complete the appraisal. This proposed loan is scheduled for Board presentation by October. The Portuguese delegation may wish to reiterate earlier requests for assistance in development finance (especially for the National Bank of Development) and in agriculture and education.

5. You will find attached, biographical notes on the members of the delegation (Annex I) and a brief on the economy (Annex II).

Attachments

cc: Messrs. Wapenhans o/r
Dubey
Maiss
de Lusignan

GdeLusignan/PSmith:ea

*concern is creditworthiness
must borrow in capital markets
prob: weakness of budget
BoT 2/14/76*

3,5

48

BIOGRAPHICAL DATA

Mr. Francisco Salgado Zenha, Minister of Finance, Governor for the Bank, born in 1923, in Braga, a town in Northern Portugal, ranks second after Mr. Mario Soares in the Socialist Party. He is a lawyer by profession, like Mr. Soares, and under the Salazar/Caetano regime he played a major role in the opposition by participating in youth movements and in the legislative elections of 1965 and 1969. During the first weeks of the Portuguese Revolution, he helped establish the Socialist Party. In May, 1974, he was appointed Minister of Justice, a position that he kept in the second, third, and fourth government reshuffled. He was asked to become Minister of Finance in the Sixth Portuguese Government.

As a Minister of Finance, Mr. Zenha is not considered a technician. While he has had exposure to banking and private business before the Revolution, in his capacity as legal counsel to several big Portuguese companies, he is essentially a politician. Mr. Zenha represents the right wing of the Socialist Party and is a major opponent to any association with the Communists or with the radical elements of the Army.

Mr. Jose da Silva Lopes, Governor of the Central Bank and Governor for the Fund. Mr. da Silva Lopes has been associated with the financial community for many years as the Director of the General Savings Bank and more recently in the Provisional Governments. He has held, since the Revolution, the positions of Minister of Finance, and Minister of External Trade. He became Governor of the Central Bank last October. He attended the 1974 Annual Meetings as Minister of Finance.

Mr. da Silva Lopes does not belong to any party. He is known as being a liberal of high intellectual integrity. His long experience in finance and banking and his earlier cabinet positions make him very influential under the present circumstances.

Mr. Victor Constancio, Secretary of State for Planning and Budget, and Alternate Governor for the Bank is 36 years old. He was a Professor of Economics at the time of the Revolution and was asked to serve as Secretary of State for Planning under Mr. da Silva Lopes in the Second and Third Provisional Governments (July '74 to March '75) and to assist Major Atunes, currently Minister of Foreign Affairs, at that time Minister of State Without Portfolio in charge of economic coordination, in preparing the economic and social policies program, known as the "emergency program", which took effect in February 1975. After that he returned to teaching and helped develop the economic plan

- 2 -

of the Socialist Party upon which the Sixth Government's action program is based. For a brief period in 1975 he was also Director of Research in the Central Bank.

Mr. Raul Capela, Adviser to the Minister of Finance, born in approximately 1935, was a member of the Board of the Banco Portuguesa Atlantico prior to joining the present Government as Adviser to Minister Zenha. He is trained in economics. He accompanied Mr. Mario Soares during his visit in Washington last January.

ECONOMIC BRIEFBackground

In the last two years Portugal has suffered serious setbacks. Production, investment and exports declined while consumption in relative terms continued to increase, thus creating a growing imbalance in domestic finance and deficits in the Current Account Balance.

	<u>1973</u>	<u>1974</u>	<u>1975</u> (Provisional)
Gross Domestic Product (real growth in %)	+12	+2	-3 to 6
Investment (real growth in %)	+12	+9	-15 to 20
Consumption (real growth in %)	+12	+4	+2 to 3
Overall budget deficit (Escudo billion) ^{1/}	-2.7	-17.3	-39.7
Exports ^{2/} (US\$ billion)	4.0	4.5	3.8
Imports (US\$ billion)	3.7	5.5	4.8
Current Account Balance (US\$ billion)	+0.3	- 1.0	- 1.0
Foreign Exchange (US\$billion, end year)	1.71	1.01	0.25

Principal Problems and Staff Assessment

Following the Revolution in April 1974, the unsettled political conditions and changes in the structure of ownership and economic institutions coincided with international price increases for Portuguese imports and depression in the economies of its major trading partners. The difficulties created by these circumstances were further compounded by the influx of refugees, demobilization of armed forces and deceleration in the rate of traditional emigration to European countries. Consequently, the post-revolution Governments, and in particular the current Sixth Government installed in September 1975, were confronted with a very serious unemployment situation (11-12 percent at end 1975), and during 1975, a decline in real GDP (3 to 6 percent) with investment down by 15-20 percent and export by 7 percent in real terms. In addition, the budgetary deficit had more than doubled to about 1.5 billion dollars (11 percent of GDP) and the current account of the balance of payments showed a deficit of about \$1.0 billion (equivalent to 20 percent of imports) in 1975.

To cope with the economic deterioration and to initiate the long-term adjustments necessary to resume growth in the economy, the present Government, immediately following its installation, formulated a comprehensive program of policies. The program consists of a package of measures designed to contain consumption and imports demand on the one hand and raise the level of investment and exports on the other.

^{1/} Including the Supply Fund covering mainly the subsidy operations.

^{2/} Goods and Services, including tourism and workers' remittances; current prices.

The likely impact of the several recent austerity measures, e.g., increases in general sales tax and upward adjustment in rates of public utilities, gasoline prices ^{3/}, transport charges and prices of several essential consumer goods, will be to reduce consumption and release some additional resources for much needed investment. This effort is being supplemented with a major reorientation of the 1976 budget - reduction in the defense expenditures (60 percent) and a substantial increase in development related expenditures (90 percent). In addition, the creation of some new institutions and reorganization of others, to respond to the changed circumstances, will facilitate the development process. These are steps in the right direction.

The financial and investment requirements of the nationalized enterprises and the gap created by the reduced activities of the private sector and foreign investment are, however, such that the present resource mobilization measures are inadequate and must be further reinforced. According to Government estimates Escudo 60 billion (or about US\$2.2 billion) a year are needed for the next five years to meet the resource needs of the nationalized enterprises. These yearly needs are more than double the total development expenditures in the current budget and about 30 percent more than the estimated gross national savings in 1974. If additional real resources are not mobilized and too much reliance is placed on the banking system, it would intensify inflationary pressures which will make the stabilization and recovery process even more difficult. The Government will, therefore, have to closely observe the impact of present policies so that it can determine the additional resource mobilization measures required and take appropriate action.

On the external side, the international community and bilateral donors have responded well to the country's resource needs by already providing about US\$640 million as balance of payments support (with the possibility of additional \$70-100 million from the IMF on account of Compensatory Financing and Supplementary Oil Facility Loans) and by committing about \$470 million for 1976-1977 for long-term project aid. Nevertheless, the Government will have to pay more attention to the level as well as the composition of imports so as to avoid the critical shortages of essential consumer goods and meet the import requirements of the development process. Similarly much more vigorous measures to promote exports (including earnings from tourism and workers' remittances) would be needed. Ultimately the competitive position of the Portuguese exports must be re-established and the shortage of foreign exchange must be reflected in its cost to the importers through an appropriate

^{3/} At \$2.75 per gallon, the gasoline price is one of the highest in the world.

adjustment of the exchange rate. The Government has an open mind on this issue but would like to assess the impact of import surcharges and sales tax increases on import demand before introducing any fundamental change in the exchange rate. No doubt, the problems of external sector - restricting and restructuring the import demand and promoting exports - can only be solved gradually but an appropriate realignment of the exchange rate will be unavoidable to achieve any tangible success in this respect.

The policy initiatives adopted by the present Government to tackle the current economic problems can justifiably be characterized as courageous and impressive when compared to the actions of the previous five governments. However, the magnitude of the task, particularly after extensive nationalization and government's direct involvement in the production process, demands further reinforcement of measures already introduced. More specifically, additional measures to mobilize resources and further steps to strengthen the project formulation and execution capabilities are needed. Similarly, to reactivate the residual private sector, the respective roles of the private and public sectors have to be clearly defined and the foreign investment code promulgated.

In view of the impending general elections on April 25, 1976 and the fact that the Presidential election, and the formulation of the new cabinet, will not take place before the end of June 1976; it is most unlikely that further austerity measures would be introduced before the second half of this year. It would be reasonable to anticipate, however, that any new government would have little maneuverability to depart from the general pattern of measures that have already been introduced.

9.

OFFICE MEMORANDUM

TO: Memorandum for the Record

DATE: December 17, 1976

FROM: Martijn J.W.M. Paijmans, Director, EMENA I PSUBJECT: PORTUGAL - Visit to Mr. McNamara by the Minister of Finance

1. On December 16 the Portuguese Minister of Finance, Dr. Henrique Carlos Medina Carreira met with Mr. McNamara. Dr. Carreira was accompanied by Dr. Jose da Silva Lopes (Governor of the Central Bank), the Portuguese Ambassador, and Mr. Pessoa (Financial Counselor at the Embassy). Mr. Rota attended the meeting. Also present were Messrs. Benjenk and Paijmans.

2. The Minister presented an overview of the measures recently taken and to be taken by the Government in the field of economic policy, starting out with an explanation of the recently reinforced (by municipal elections) position of the Government in spite of the unpopular economic measures it had taken. He explained that the Government:

- is determined to take further stabilization measures,
- has announced that no further nationalization will take place,
- has presented to Parliament a law defining the scope of private activity in Portugal,
- has taken measures to improve productivity of labor by allowing action against absenteeism and dismissal of redundant members; further action on regulating working time will be presented to Parliament,
- is
- /defining a regime for enterprises in difficulties that will waive for them the existing Collective Agreements thus allowing for lower salary cost,
- is proceeding to return land illegally taken to the rightful owners,
- intends to make changes in the pricing policy to adjust prices to more realistic levels (in transportation, prices already went up 25% to reduce public enterprise deficits), among others by removing items from the list of controlled prices.

3. The Minister said that the new budget presented to Parliament incorporates strong reductions in the current account deficit of the public sector, including the social security system (a 50% reduction in nominal terms, 60% in real terms). The Central Government's current budget deficit, in nominal terms, would next year be the same as last year's but smaller in real terms. The reduction was to be achieved by:

December 17, 1976

- cuts in subsidies and transfers,
- increased sales tax and social security premiums,
- improved tax collection.

The Government is also preparing action on interest rate policies and is studying an average increase of about 2 percentage points.

4. The Minister hoped for continued Bank assistance and mentioned particularly the need for advice on policies and technical improvements in the agricultural sector, and for assistance to the export industry. He expressed the appreciation of the Government for the support of the Bank and the work being done, not only in terms of resource transfers but also and particularly in terms of advice and technical assistance.

5. Mr. McNamara congratulated the Minister and, through him, the Government on its political courage to design and implement a program aimed at reducing consumption, increasing savings and investment, and expanding exports, thus reducing unemployment. He indicated that the Bank firmly supports these objectives and is anxious to discuss their economic framework in January when our draft economic report will be the subject of meetings in Lisbon.

6. In response to Mr. McNamara's enquiries, the Minister and Dr. da Silva Lopes explained that inflation would remain high at 15-20% next year--according to the Ministry of the Plan--also because of the impact of corrective measures to achieve realistic price levels. The Minister indicated that about 125,000 new jobs will be created in the public sector next year [Note: this would reduce unemployment from the current 15% to 11-12%] with a possible effect on private sector employment as well. In response to a question on export prospects the Minister and the Governor said that Portugal had spare capacity for 2-3 years of export expansion.

7. Mr. McNamara thanked the Minister for his explanations, said he would be waiting for the results of the economic policy discussions in January, and indicated the Bank's readiness to provide financial and technical support. The amount of lending would of course depend on the measures taken by the Government. The Minister invited Mr. McNamara to visit Portugal.

cc: Mr. McNamara's office (original and one carbon)
Messrs. Benjenk
Knox
Aiyer
Kavalsky

MPaijmans:gg/sap

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara
THROUGH: Mr. J. Burke Knapp
FROM: Munir P. Benjenk

DATE: December 15, 1976

SUBJECT: PORTUGAL: Meeting with Minister of Finance and Governor of Central Bank

1. Attached is a brief for your meeting with Dr. Henrique Carlos Medina Carreira (Minister of Finance) and Dr. Jose da Silva Lopes (Governor, Central Bank) on Thursday, December 16, at 6:00 p.m.; short biographical notes on them are also attached.

2. We understand that the main purpose of their visit to Washington is to formally finalize the borrowing of \$300 million out of the Exchange Stabilization Fund from the U.S. Treasury. The visit was arranged hurriedly as Undersecretary Yeo had to cancel his proposed visit to Europe. We expect that the Portuguese may use the opportunity to touch upon the proposed multinational \$1.5 billion balance of payments assistance package being put together by the U.S. Government, although we are informed by the U.S. State Department that the U.S. officials are not in a position to add anything on this until after they obtain a 'sense of the Congress,' around mid-January, 1977. In any case, general discussions were held by a U.S. Treasury mission in Lisbon two weeks ago when the Portuguese had agreed that they would have to reach an understanding with the IMF on economic measures as a condition of the aid package. The Minister of Finance and his colleague are expected to arrive on Wednesday night and spend most of Thursday in discussions with the Treasury. They will also be meeting the heads of the IMF and EXIM Bank before leaving on Friday.

3. A brief review of the economic situation, recent political developments and the progress of our operational and economic work in Portugal follows.

Recent Political Developments

4. The political instability experienced by Portugal since the April, 1974 revolution, characterized by six changes in Government, seems to be coming to an end. This change has been marked by the following five events:

- a. Promulgation of the new Constitution, drafted by the Constituent Assembly, in early April 1976;
- b. Election of the Legislature, with the Socialists winning a plurality of 35 percent on April 25, 1976;
- c. Election of General Antonio Ramalho Eanes as President of the Republic on June 28, 1976, by 61 percent of the votes cast;

- d. Mr. Soares' (leader of the Socialist Party) appointment as Prime Minister in July 1976; and,
- e. The recent December 12, 1976 Municipal elections, which indirectly reaffirmed support for the Socialist Party by giving it overall a 33 percent plurality.

As a result of these developments, especially the last one, it would appear that:

- i. The significance of the Armed Forces has been considerably reduced, and a legitimate, democratically elected government holds power in Lisbon and is attempting to work through a parliamentary system;
- ii. The pressure on Premier Soares to form a coalition with the left or the right is abated;
- iii. Premier Soares should be able to pursue his program of economic austerity and rehabilitation with more confidence.

Economic Situation

5. Portugal's economy is still adjusting to the vast post-1974 revolution changes: land reforms affected 23 percent of cultivable area; nationalization of banking, insurance, and large industrial groups extended the public sector to cover 27 percent of GDP; trade union activity became significant and minimum wages and social security benefits were greatly expanded. In addition, the recession in the OECD countries adversely affected Portuguese exports (60 percent go to industrialized Europe) and tourist receipts and remittances from the one million Portuguese (a third of the labor force) working abroad. Conditions were aggravated by import price increases (e.g., oil added \$400 million to 1974 import bill), the decolonization process and loss of 10 percent of export markets, and the repatriation of 800,000 Portuguese (8 percent of mainland population). For the economy and the society to absorb these fundamental changes and to be restructured will take a long time.

6. As at end-1976, Portugal's economy is in the grip of stagflation. GDP declined by about 3 percent in 1975, and there is not likely to be much improvement in 1976. High overall consumption reduced domestic savings to a negative level in 1975 and pushed down national savings to 6 percent of GDP -- the lowest rate in Europe. Investment was reduced to 9 percent of GDP in 1975. The budgetary gap in 1975 and 1976 enlarged to about 8 percent of GDP and about 50 percent of the budgetary receipts. Central

Bank financing of the large public sector deficit, rapid increases in wages and salaries, and a decline in productivity have led to rapid inflation -- about 20 percent per annum in 1974-75 and about 25 percent in 1976. The balance of payments current account worsened from about \$300 million surplus in 1973 to a deficit of \$1.3 billion in 1976. The most serious feature is the high level of unemployment: 15 percent in 1976 (over half a million unemployed).

Austerity Measures

7. Several austerity measures were introduced in late 1975 and early 1976, and by the Soares Government in July 1976, the main objective of which is to contain consumption. The measures fall into three categories: raising the controlled maximum prices, increasing indirect taxes and social security contributions, and restricting payroll increases to 15 percent per annum. To improve the balance of payments, surcharges and restrictions were intensified, the exchange rate was allowed to depreciate about 14 percent during the first half of 1976, and trade concessions were negotiated with the EC and EFTA. While the measures introduced were in the right direction, the continuation and, in some respects, the worsening of problems in 1976 make it clear that they are not enough. The level of overall consumption is still very high, the share of savings is depressingly low (national savings 6 percent of GDP, domestic savings negative) and so are investments (10 percent of GDP). The financial imbalance in the public sector is at an all-time high, inflationary pressures persist, and the balance of payments deficit has become a critical constraint. Free foreign exchange reserves have declined to a dangerously low level (less than one month's import at end 1976) and one-third of the 28 million ounces gold stock has been pledged as collateral for borrowings abroad. Above all, unemployment has escalated to an unprecedented level.

Bank Staff Position

8. We feel that the keys to an effective response to the present economic situation are:

- a. Reducing inflation to 15 percent in 1977, 10 percent in 1978, and limiting it to the international rate thereafter;
- b. Containing growth in real consumption by reducing private consumption by removing price controls, limiting wage increases to 10-15 percent per annum, reducing budgetary deficits and food subsidies, raising taxes and increasing the savings of public enterprises;
- c. Encouraging private savings by allowing tax exemption for interest income and by raising interest rates, which are highly negative;
- d. Raising level of public investment and carrying out economic analyses of projects;
- e. Improving the balance of payments situation through an adjustment in the exchange rate, special tax incentives to exporters and

through economic import subsidies, particularly in agriculture; and,

f. Designing specific employment programs.

9. The economic report (to be sent to Portugal in green cover by end-December) will dwell on these themes and discuss alternative policy approaches entailed. A mission to be joined by Mr. Paijmans will discuss the report and its recommendations with the Portuguese authorities during January 1977.

10. We are informed that Premier Soares is under constant pressure from President Eanes to give top priority to reversing the decline in the economy. We understand that, as a quid pro quo for the \$300 million short-term aid, the U.S. Treasury mission asked for, and the draft 1977 budget, now being discussed by Parliament, reflects an increase in development expenditures, a reduction in current expenditures in real terms and a narrowing of the budgetary deficit. This would indicate that the Government is willing to continue the tight program. Now that the Municipal elections are over, we hope that it will be possible for the Government to sustain its focus on the important measures needed to put Portugal back on the growth path in two to three years.

Bank Activities

11. We have mounted a fairly intensive economic work program for Portugal; an economic report was distributed July 1975; and, as mentioned earlier, the green cover report of the last mission (August 1976) will be sent to Portugal by end December 1976. Our project and sector work has not, however, progressed equally satisfactorily. Internal uncertainties in Portugal aroused apprehensions in the Bank, and delayed and staggered the Region's preparatory work on the development of a lending program. In March 1976, the lending program was reviewed again, and the Region was then authorized to proceed with on-going work and to commence identification and preparation work on the attached lending program.^{1/} The pace of our project preparation has picked up considerably thereafter. A DFC project was appraised in October 1976 and is scheduled for Board consideration in May 1977, and the following sector studies and project identification missions have been undertaken or scheduled:

- a. Water Supply and Sewerage: WHO/Bank Sector Survey Mission: September-October 1976; and a Bank Project Identification Mission scheduled: January 1977;
- b. Agriculture and Rural Development: Bank Sector Survey and Project Identification Mission: October-November 1976; and FAO/Bank Agricultural Credit Project Preparation Mission scheduled: February 1977;

1/ A \$36 million Power loan was approved in June 1976, and a \$24 million Highway loan was approved in October 1976.

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- c. Education: Project Identification Mission: November-December 1976;
- d. Transportation: Technical Assistance provided under Highways I project will help to prepare further highways and railways projects;
- e. Industry: In response to the Government's request at Manila, we have agreed to schedule a Sector Survey Mission in the spring of 1977.

12. The Portuguese officials have rendered excellent cooperation to the missions, and, more importantly, been very willing to discuss recommendations for reform. The missions have consistently reported a clear readiness to reform at the sectoral level, and that the officials are keen to secure Bank advice and support for planning and implementing the changes. The missions have also emphasized the pressing need for structural and institutional reform, to adapt to the new situation and to modernize Portugal. The approved country program envisages lending of about \$75 million through three projects a year. The next CPP on Portugal is scheduled for your review in March/April 1977, and we may, at that time, propose an increase in the level of lending if the developments in Portugal and the state of project preparation support such an increase.

13. Mr. Aiyer, the Programs Division Chief, will join Bank staff in Lisbon tomorrow to discuss operational matters aimed at advancing the project preparation efforts (particularly for the FY78 program, which could include agricultural credit and education) and our concerns on the policy issues regarding the proposed DFC operation (FY77), where the major problems pertain to the negative interest rates, and the need for a clear articulation of the Government's policies for development of the industrial sector. Also, we understand that the Central Bank is considering a scheme whereby sub-borrowers would not bear the exchange risk; the details have apparently not yet been decided upon (your meeting might provide an opportunity to stress to the Governor our strong feeling that scarce foreign exchange should be priced appropriately and that sub-borrowers should ideally bear the exchange risk).

*Delegation by
JBY*

Matters to be Mentioned

14. You may wish to assure your visitors that we do realize that the Government has been treading a tightrope until now, making it difficult to take each and every one of the austerity measures needed. However, we hope it will now be possible for them to sustain their focus on rehabilitating the economy as long as necessary. We plan to support these efforts through our project and sector work, and would hope that our economic reviews will provide help by airing the problems as we see them and the options available to resolve them.

Attachments

SAWMoini/FMChaudhri/MSAiyer:pl:cf

Biographical Notes

Dr. Medina Carreira : Minister of Finance since August 1976

He is about 46 years old; a lawyer by profession, and has built up a reputation as an expert in taxation law. In October 1974 he joined the Board of the Intercontinental Bank of Portugal. He was Undersecretary of Treasury under Finance Minister Zenha from October 1975 to July 1976. In August 1976 when he was appointed Minister of Finance, the Ministry was reduced with the Secretariat of Economic Planning becoming a separate Ministry under Dr. Sousa Gomes.

Dr. Jose da Silva Lopes : Governor of the Central Bank

Mr. da Silva Lopes has been associated with the financial community for many years as the Director of the General Savings Bank and more recently in the Provisional Governments. He has held, since the Revolution, the positions of Minister of Finance, and Minister of External Trade. He became Governor of the Central Bank in October 1975.

Mr. da Silva Lopes does not belong to any party. He is known as a liberal of high intellectual integrity. His long experience in finance and banking and his earlier cabinet positions make him very influential.

1974 Population : 8.57 million
 (1973) GNP Per Capita : \$1410
 Population Growth Rate: 0.9%
 Exchange Rate : US\$1 = 25.4 escudos (1974)

PORTUGAL: ACTUAL AND PROPOSED PROGRAM OF LENDING OPERATIONS THROUGH FY1980
 (US\$ million)

	Through 1975	Program				Totals 1969-73	Totals 1974-76	Totals 1976-80	Reserve Projects
		FY76	FY77	FY78	FY79				
Agricultural Credit					25.0 *				
Irrigation (unidentified)						35.0			
Livestock						15.0 *			
Rural Development					20.0				
Education I				30.0					
Education II									
DFC I			30.0					30.0 (80)	
DFC II				30.0					
Highways I									
Highways II			20.0						
Railways				35.0					
Port I - V	57.5			30.0 *					
Port I		30.0							
Water Supply and Sewerage (unidentified)						25.0			
LENDING PROGRAM									
IBRD Number		30.0	50.0	95.0	75.0	75.0			
Lending Program in Constant FY74 \$ Million		1	2	3	3	3	175.0	225.0	
Commitment Deflator		19.9	31.6	57.0	42.9	40.8	6	12	
		150.4	158.4	166.4	174.7	183.5			
Standby Projects									
IBRD Number			30.0	35	30.0	-			
			1	1	1				

* Standby

10

OFFICE MEMORANDUM

TO: Memorandum for the Record

FROM: Martijn J. W. M. Paijmans, Director, EMENA I

SUBJECT: PORTUGAL - Dr. Soares' Visit to Mr. McNamara

DATE: April 22, 1977

1. On April 2, 1977 Portugal's Prime Minister Soares visited Mr. McNamara. He was accompanied by Dr. Medeiros Ferreira, Minister of Foreign Affairs; Dr. da Silva Lopes and Dr. Ribeiro Constancio, Governor and Vice Governor of the Central Bank, respectively; H.E. Joao Hall Themido, Portuguese Ambassador; and Mr. Cabral Pessoa, Financial Counselor at the Embassy. Messrs. Rota, Knapp, Benjenk and Paijmans were present.
2. The Prime Minister explained that Portugal had been on the brink of collapse but had succeeded to pull back. He explained that although the political situation gave him no cause for concern, the economic situation did. What the Portuguese economy needs now is a minimum of growth. He mentioned the discussions he had had in the U.S. on medium term loans to help settle the balance of payments problem, and highlighted the understanding and support he had received from the President of the U.S. and from the Foreign Relations Committees of both the House and the Senate. Dr. Soares also expressed gratitude for the cooperation and support of the Bank and for the good relations which had been built up. He mentioned the appointment of a new Minister for Industry and the return to Portugal of managers who had previously left the country.
3. Mr. McNamara observed that Portugal was still close to the danger point and that the Bank was fully prepared to do the utmost to help. He mentioned the constructive and close cooperation the Bank enjoys with the leaders of the Central Bank. He outlined a number of actions the Bank is undertaking in Portugal, observing that these are consistent with the Government's objectives. Mr. McNamara specifically made the point that if the Bank was not doing what the P.M. felt the Portuguese economy needed, he should let Mr. McNamara know. He added that the Bank also tried to be helpful in accelerating the preparatory process of Portugal's entry into the E.C. which, among other, would create a great stimulus for the efficiency of the country's industrial sector.
4. Dr. Soares mentioned that the future entry into the E.C. had provided the Portuguese people with a focal point for their destiny. Immediately following the revolution there had been a long period of uncertainty as to which direction the country would go - this had now been clarified. He said that in his discussions with other governments on this and related subjects, he had made use of the Bank's economic report on Portugal which he felt gave him a very favorable picture of the country's position. The P.M. ended by announcing that Dr. Ribeiro Constancio had been appointed Chairman of the Commission for European Integration.

MPaijmans:gg

cc: Mr. McNamara's office (original and one carbon)
Messrs. Knapp, Benjenk, Aiyer

Form No.
(2.66)

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT
ASSOCIATION

INTERNATIONAL FINANCE
CORPORATION

ROUTING SLIP

Date
April 19

OFFICE OF THE PRESIDENT

Name

Room No.

Mr. McNamara

4/19

To Handle

Note and File

Appropriate Disposition

Note and Return

Approval

Prepare Reply

Comment

Per Our Conversation

Full Report

Recommendation

Information

Signature

Initial

Send On

Remarks With reference to paragraphs 10 and 11 of the attached briefing memorandum on Portugal, it seems to me that we should work with OECD countries and private banks on project financing in Portugal, but I doubt if we should try to play a role in the short-term aid mobilization effort, beyond perhaps offering our technical economic services to any meeting that may be set up in Paris.

From

J. Burke Knapp

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara, President
 THROUGH: Mr. J. Burke Knapp, Senior Vice President, Operations
 FROM: Munir P. Benjenk, Vice President, EMENA Region

DATE: April 18, 1977

SUBJECT: PORTUGAL: Meeting with the Prime Minister

General

1. This memorandum sets out some background material additional to that in the Portugal CPP dated April 4, 1977, for your meeting with Dr. Mario Soares, Prime Minister; Dr. Jose da Silva Lopes, Governor, Central Bank; and Dr. Victor Constancio, Vice-Governor, Central Bank, on Thursday, April 21, at 5:30 p.m. They will be accompanied by Ambassador Joao Hall Themido and Mr. A. Cabral Pessoa, Financial Counselor to the Embassy. Short biographical notes on the Prime Minister and members of the delegation are given in Annex I.
2. We understand that the main purpose of the Prime Minister's visit to Washington is for discussions on: (a) the proposed multinational aid package that the U.S. Government has been trying to put together for Portugal; (b) further U.S. Government assistance which, for FY77, would be about \$65 million for security support; \$50 million for PL 480 Title I and \$20 million in Housing Investment Guarantees; and (c) future financial aid from the IMF.
3. You last met with Portugal's Finance Minister Carreira ^{1/} and Governor Silva Lopes on December 16, 1976 when they were here to discuss a \$300 million short-term (6-month) loan from the U.S. (Exchange Stabilization Fund). At that meeting you mentioned the importance you attached to the Bank's macro-economic policy discussions on the basis of a draft economic report and which were scheduled for January 1977. Mr. Paijmans and a team from the Programs Department had very fruitful discussions and found a broad basis of agreement in Portugal with the Bank's assessment and proposed areas for action. Subsequently, in February the Government introduced an economic policy package (see paragraph 6 below) which was fully in line with suggestions made by the Bank. Dr. Silva Lopes announced this quite satisfactory package to you in a cable to which you responded in a congratulatory manner.
4. Prime Minister Soares is also coming to the United States to accept an award in New York for his "support of human rights." We understand that, of late, he has developed considerable stature in Europe, and, during his recent visits to various European capitals soliciting support for Portugal's entry into the EC, government leaders were very favorably impressed with his qualities. The people accompanying him (and Finance Minister Carreira) are considered his top economic advisors. (The Minister of Foreign Affairs, Mr. Jose Medeiros Ferreira, and Mr. Rui Mateus, the Economic Advisor to the President, are also visiting the United States with the Prime Minister and are likely to also come to the Bank, as they are accompanying Mr. Soares to all the other meetings.)

^{1/} The Finance Minister was to be part of the delegation but fractured his leg last week and therefore dropped out.

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Recent Developments

5. After the latest CPP to be reviewed on April 21 was distributed, the Prime Minister reshuffled his Cabinet by: appointing a new Minister of Industry reputed to be a capable manager and technocrat and a new Minister of Commerce and Tourism; and confirming the dynamic and moderate Minister Barreto in the Ministry of Agriculture (a position held until mid November by the leftist Lopes Cardoso). Mr. Barreto has been working actively towards revamping the sector and correcting the more extreme and illegal steps taken since the Revolution such as the forcible occupation of farms in the south. The result of the Cabinet shuffle is seen as a further rightward shift by the Socialists. The appointment of a former businessman in the Ministry of Industry is aimed at restoring confidence in the private sector.

6. In a continuing effort to address the unemployment and balance of payments problems the Government has moved decisively in February 1977 as explained in paragraph 26 of the CPP to:

- (a) Improve the balance of payments through reduced imports, and a 15 percent devaluation of the escudo in February 1977 to encourage exports, tourism and workers' remittances.
- (b) Contain consumption through increased taxes, reduced subsidies, and increased utility rates while at the same time controlling wages and incomes.
- (c) Increase employment through an expanded public investment program and encouragement to private sector and foreign investors.

As explained in paragraph 30 of the CPP, the Government has also been working on mobilizing external capital such as the short-term loan of \$300 million from the U.S. and the proposed multilateral aid package of about \$1.5 billion (see paragraph 8). Furthermore, the IMF has already granted \$200 million from the oil facility and compensatory financing and its Board will consider on April 25, 1977 the first credit tranche amounting to \$49.0 million. We now understand that the Portuguese have also asked and are expected to receive in July a drawing from the IMF as compensatory financing and possibly a second credit tranche later in the year. Given the fact that Prime Minister Soares' Socialist Party only commands a one-third plurality in Parliament, it deserves commendation for taking the bold and stiff economic policy measures announced in February 1977 and for its resolve in persisting with and reinforcing the austerity program. You may wish to add that we will continue to assist in any way we can in support of the Government's further efforts to revive growth with relative price stability.

Entry into Europe

7. Portugal formally applied to the EC for membership on March 29, 1977 and is initiating measures to prepare the economy for eventual integration into the EC. We have learned from the EC (in Brussels) that they do not want

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negotiations with Portugal to be as drawn out as those with Greece. To this end, they have asked that, in making adjustments, Portugal be careful to try to ensure that the effects of any policies implemented for entry into Europe not have an adverse impact on the domestic economy, and equally, that the effect of any policies to correct domestic economic problems not have an adverse impact on entry into Europe. So far, little work has been done either in Lisbon or in Brussels on the implications of Portugal's entry into the EC. (Besides the Bank, only the OECD has done analysis of medium-term relevance.) In fact, EC staff have called on Bank staff asking for our analysis of the issues involved. We hope to cover in the course of future economic work some of the key problem areas related to the proposed integration (to the extent the budget permits). You may wish to ask the delegation if there are particular problems of concern to them which they would like us to study -- from our point of view and expertise.

Multinational Aid Package

8. The Prime Minister may raise this subject with you. Around November, 1976, at the request of the Portuguese, the United States began to organize a US\$1.5 billion aid package to provide support to Portugal over a 3-year period. The original proposal was that the United States would provide about 40 percent of this aid, and that other OECD countries including Japan, would contribute the rest. The funds were expected to be disbursed over three years and repaid over a 5-year period including one year of grace. The funds from this package were to be available only after Portugal becomes eligible to draw from the IMF in the higher credit tranches with loans phased to supplement the IMF drawings and to be suspended when IMF eligibility to draw was suspended. It has been reported that President Carter personally wrote to the leaders of other prospective participant countries, such as West Germany, France, Japan, Netherlands, Canada. The IMF was expected to administer this in terms of setting the conditions and disbursing the funds.

9. The Bank has not been involved, by the United States, in organizing the US\$1.5 billion aid package. The IMF has, however, played a central role in terms of defining policy measures that Portugal needs to take to qualify for this aid. This is evident because: (a) the aid package was conceived originally as a purely balance of payments support, and (b) Portugal is seen as a part of Western Europe, where traditionally the IMF has been more visible on the economic front. Nevertheless, since Portugal's economic situation has of late been dominated by short-term problems our economic discussions in January 1977, covered short-term problems in addition to those of a more medium- or long-term nature; we have attempted to work in close coordination with the IMF. This approach is approved by the Central Bank which has consistently stated that it welcomes whatever we can do mainly because of our not losing sight of the medium- and long-term.

10. We have very recently learned that the West Germans, in particular, and also the Japanese do not support the U.S. proposal for a 3-year program of balance of payments assistance. The Germans reportedly feel that they have done quite much through gold collateral loans extended by the Deutsche

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Bundes Bank (about US\$300 million equivalent). Apparently, Chancellor Schmidt has told Prime Minister Soares about West Germany's hesitation to commit itself to a 3-year package. We understand that the Germans feel that the proposed new IMF "Facility" would, if established, be the better instrument for providing aid for the second and third years to Portugal. Finally they are not certain that balance of payments support would be better than project and investment aid. The U.S. Treasury is now talking to all the other prospective participants and, on the basis of discussions to date, has decided to cut the program back to a one-year exercise for US\$700 million, of which the share of the United States would be 40 percent. Pending conclusion of these discussions the Authorization Bill has not yet been submitted to the U.S. Congress. The U.S. Treasury has very recently indicated (informally at the staff level) that after the bilateral discussions they may approach the IMF and the Bank formally to ask for a meeting chaired by both in Paris (possibly as early as next month) to discuss the proposed one-year aid package with all prospective participants. During Prime Minister Soares' visit, the United States expects to voice its strong support for the aid package, and to undertake to move forward as best as it can. Mr. Soares is expected to ask for U.S. pressure on the other donors. He will also ask for support from the IMF and, very likely, the Bank in their effort to mobilize aid.

11. You may wish to indicate to Prime Minister Soares that our own projections clearly demonstrate that Portugal needs sizeable amounts of external funds (about US\$850 to US\$900 million per year) for the next three years, based on a set of assumptions which were discussed with the Government last January (these are reflected in the CPP). You may also like to express satisfaction of the fact that the OECD countries have decided to come to the aid of Portugal, and if the Government would desire, offer the Bank's assistance in this particular aid mobilization effort. It might also be useful to link this subject to our interest in acting as a catalyst for financial assistance from other sources (including private banks) for projects which we prepare for Bank financing. We feel that, for Portugal, this will have to be mainly official bilateral aid from European countries and the United States and Japan, and the capital market. (The Portuguese are discussing with the European countries, the subject of project financing, besides the aid package). The EIB has informally indicated that it would like to continue working with the Bank on projects for its future financing.

Recent and Proposed World Bank Activities

12. With reference to Bank activities you may wish to express appreciation for the excellent cooperation all Bank missions have received, and note that our active economic sector work and proposed lending program (see Annex II) will necessarily have to be tied closely to continued progress on the economic front.

13. Annex II contains details of the ongoing and proposed lending operations. We are seeking in the CPP approval for a lending program of about \$85 million for three projects per year. There is no doubt that Portugal, given its creditworthiness and absorptive capacity, could absorb much larger

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amounts of Bank lending. In this regard, it should also be pointed out that its 1975 per capita GNP following this year's devaluation would actually be about US\$1,370 in 1977 dollars using the World Bank Atlas methodology, and US\$1,114 at the current exchange rate. An updating economic report entitled "Portugal, An Economy in Transition," Report No. 1408a-PO, was issued to the Executive Directors on March 16, 1977. Further economic updating work is not programmed until the fall of this calendar year when a mission to review the medium-term plan will visit Portugal. An economic updating mission is scheduled to visit Portugal in April/May 1978. An agriculture sector mission visited Portugal in October 1976, and a draft report will be discussed with the Government around September 1977. The report identifies that agriculture credit, livestock, irrigation, fisheries and rural development are the areas most in need of further development and external assistance in the coming years. A Bank tourism mission visited Portugal in March 1977, and its report is likely to be discussed with the Government in July 1977. An industrial sector mission is scheduled to arrive in Portugal on April 26, 1977. The mission will focus, in particular, on ways to stimulate exports. This assistance was requested by Dr. Silva Lopes during last year's Annual Meeting discussions.

14. We are also, at the special request of the Government, in the midst of providing assistance towards reassessing the whole US\$3.0 billion Sines Industrial Complex conceived in Salazar's days, and which now seems economically unviable. We are assisting in drawing up the terms of reference for a complete re-evaluation^{of the} complex. As the complex has not been subjected to a rigorous evaluation since the oil price increase, it is hoped that this review will help the Government re-phase the development to more closely meet current conditions. In view of the Government's interest to proceed on this re-evaluation and the budgetary constraints of the World Bank, the Central Bank is paying a part of the expenses and consultant fees for this mission.

Project Evaluation

15. At the request of the Ministries of Planning and Industry and the Banco de Fomento Nacional, we are assisting them in the development of expertise in the calculation of the financial and economic rates of return and shadow price methodology. We have already supplied a considerable amount of material to the Portuguese on project preparation and evaluation and a small mission will visit Lisbon to advise on training courses for this purpose.

Compensation for Nationalized Assets

16. The Government has been making steady progress on this, and announced in February 1977 that, by end April, 1977, it will determine the amounts to be paid to foreign shareholders. You may wish to mention the importance of reaching satisfactory settlements at an early date in order to increase private investor confidence.

17. From meetings held in Lisbon and in Washington between Government officials and Mr. Broches and members of his staff, we understand that the Portuguese are seriously considering the possibility of joining ICSID as part of their effort to encourage foreign private investment, although no decision has yet been reached.

Attachments

PESmith/SAWMoini/MSAiyer/MJWMPaijmans:stv:pl

BIOGRAPHICAL NOTES

Dr. Mario Soares: Prime Minister since July 1976

Dr. Soares is 53 years old and a lawyer by training. In 1970 he was forcibly exiled from Portugal and lived in France until the April 25, 1974 revolution. He was Secretary-General of the Socialist Party and held various portfolios in several Governments until asked by President Eanes in July 1976 to form a Government.

Dr. Medina Carreira: Minister of Finance since August 1976

He is about 46 years old; a lawyer by profession; and has built up a reputation as an expert in taxation law. In October 1974 he joined the Board of the Intercontinental Bank of Portugal. He was Undersecretary of Treasury under Finance Minister Zenha from October 1975 to July 1976. In August 1976 when he was appointed Minister of Finance, the Ministry was reduced with the Secretariat of Economic Planning becoming a separate Ministry of Plan and Economic Coordination (under Dr. Sousa Gomes).

Dr. Jose da Silva Lopes: Governor of the Central Bank

Dr. Silva Lopes has been associated with the financial community for many years as the Director of the General Savings Bank and more recently in the Provisional Governments. Since the Revolution, he has held the positions of Minister of Finance, and Minister of External Trade before he became Governor of the Central Bank in October 1975.

Dr. Silva Lopes does not belong to any party. He is known as a liberal of high intellectual integrity. His long experience in finance and banking and his earlier cabinet positions make him very influential.

Dr. Silva Lopes is the contact point in Lisbon for the Bank (and the IMF) and has provided us with active support.

Dr. Victor Constancio: Vice Governor, Central Bank

Dr. Constancio is 37 years old. He was a Professor of Economics at the time of the Revolution and was asked to serve as Secretary of State for Planning under Dr. Silva Lopes in the Second and Third Provisional Governments (July 1974 to March 1975) and to assist Major Antunes, at that time Minister of State Without Portfolio in charge of economic coordination in preparing the economic and social policies program, known as the "emergency program", which took effect in February 1975. After that he returned to teaching and helped develop the economic plan of the Socialist Party upon which the Sixth Provisional Government's action program was based. For a brief period in 1975 he was also Director of Research in the Central Bank. During 1976 he has contributed substantially to the formulation of the Government Program presented to the legislative assembly by the Prime Minister, Mario Soares. After a brief period as the Majority Leader in Parliament (where he defended the Socialist Party's stringent austerity measures) he assumed the position of Vice-Governor at the Central Bank responsible for negotiating Portugal's entrance into the EC. He continues to advise the Prime Minister on economic policies.

STATUS OF OPERATIONS PROGRAM

FY1976

Power VI

\$36.0 million approved in June 1976.

FY1977

Highways (\$24.0 Million):

Approved by the Board of Executive Directors on October 19, 1976 this loan was signed on March 3, 1977 after delays resulting from the Government's decision to secure Parliamentary approval for the draft legal documents. The loan finances road rehabilitation and maintenance in the Lisbon region and technical assistance to develop: (i) the first multi-modal transport plan; (ii) a national highway maintenance and rehabilitation program; and (iii) a railway rehabilitation program. The technical assistance is expected to lead to future Bank loans for both highway and railway development.

Banco de Fomento Nacional (BFN):

Negotiations for a proposed \$35.0 million loan to a government owned national development bank (BFN) will begin April 18, 1977. The proposed loan will finance about 35 percent of the foreign exchange requirement during the 1977-79 period for direct investment credits -- principally to small and medium size enterprises. The objectives of the loan are to: (i) provide an immediate resource transfer along with the expectation of serving as a catalyst for other foreign lending; (ii) assist BFN to improve its appraisal and supervision capabilities; and (iii) to the extent possible encourage investment in export and employment oriented industries and thereby help with the two key problems faced by Portugal, namely, balance of payments and unemployment. The loan is scheduled for consideration by the Executive Directors in late May, 1977.

FY1978Water Supply:

In January and April 1977 a preparation mission visited Lisbon to review the final preparations for a water supply project to supply water to the Lisbon region via a 70 km water pipeline, from a reservoir to the north of the city. The water is urgently needed to augment current low quality supplies from nearby rivers and underground sources. The loan amount is likely to be about \$30.0 million. Appraisal is scheduled for mid-May 1977 and Board presentation in the third quarter of FY78. This project will also enable a significant infusion of technical and management assistance and institution building.

Education:

In early April 1977 a preparation mission visited Lisbon to discuss the final steps necessary to prepare an education project for appraisal in mid-June 1977. The preparatory work is well underway and the project will focus on post-secondary technician training, teacher training, curriculum development, and general improvement of facilities. Board presentation of the loan, likely to be about \$35.0 million, is anticipated in the third quarter of FY78.

Agriculture Credit:

A FAO/CP preparation mission visited Lisbon in February and will return in June 1977 to complete preparation of an agriculture credit project scheduled for appraisal around August 1977 (as a standby). The loan of about \$25.0 million would support livestock, general agriculture and coastal fisheries investments. There is no institution responsible for agriculture credit in Portugal and the proposed project could be a first step towards the eventual establishment of a credit institution geared to agricultural development. Board presentation is tentatively scheduled for the fourth quarter of FY78.