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## PROBABLE DEVELOPMENTS IN GUATEMALA

*Submitted by the*

### DIRECTOR OF CENTRAL INTELLIGENCE

*The following intelligence organizations participated in the preparation of this estimate: The Central Intelligence Agency and the intelligence organizations of the Departments of State, the Army, the Navy, the Air Force, and The Joint Staff.*

*Concurred in by the*

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## PROBABLE DEVELOPMENTS IN GUATEMALA<sup>1</sup>

### THE PROBLEM

To estimate: the strengths and weaknesses of Guatemala; probable Guatemalan policies and courses of action; and prospects for Guatemalan stability, with particular reference to the stability of the Castillo regime.

### CONCLUSIONS

1. Many Guatemalans are passionately attached to the democratic-nationalist ideals of the 1944 revolution which overthrew the Ubico dictatorship. However, few understand the processes and responsibilities of democracy. A keen sense of nationalism, largely directed at foreign investors, colors Guatemalan politics. Responsible democratic government is therefore difficult to achieve. (*Paras. 12-13*)

2. President Carlos CASTILLO Armas still rules by decree pending the promulgation of a new constitution and the election of a Congress. He has a substantial residue of personal popularity throughout the country despite his inexperience and frequent spells of indecision. He has attempted to follow moderate policies and has placed national interests first. (*Paras. 19, 23-25*)

3. The most immediate of Castillo's problems stem from depressed coffee prices and from the effect of drought conditions

on corn, the staple diet of Guatemala. Castillo's difficulties have been further complicated by poor management, and by the impatience of the articulate sector of the electorate for a return to constitutional government. The Church-State issue has been revived during the drafting of a constitution, and is likely to prove a source of political dissension in the coming months. (*Paras. 21-22*)

4. The remainder of 1955 and the first few months of 1956 will be especially difficult for Castillo. The government's ability to survive will probably be determined by the effectiveness of Castillo's leadership, by the amount of US assistance and support, and by the international coffee market situation. Much will also depend upon Castillo's success in creating a political organization which will give his government adequate support. Favorable developments in these areas would tend to assure the loyalty of the armed forces. On balance, we believe that if economic conditions do not further deteriorate, Castillo will probably be able to remain in power during this period. (*Paras. 41-43*)

<sup>1</sup>This estimate supersedes NIE-84, "Probable Developments in Guatemala," published 19 May 1953.

5. The armed forces continue to be essential to the survival of the regime. Many of the regular elements of the army probably remain somewhat dissatisfied, but there is little likelihood of their initiating an organized rising. In the unlikely event that any of the more popular exiled army leaders were to launch a rebellion, the bulk of the army would probably remain loyal to Castillo and would be able to cope with the situation unless Castillo's political position had seriously deteriorated and the rebellion were conducted on a substantial scale. If rightist extremists among the Liberation elements in the army were to attempt a coup, it would probably be put down by the integrated regular and Liberation forces. Nevertheless, we believe that there will continue to be sporadic unsuccessful attempts against the government. (Paras. 27, 29-30)

6. Communist and Arbencista subversive activity — both domestic and foreign — has not been a serious threat to the Castillo government. We believe that the Communist and Arbencista threat at

least in the short term will remain of relatively little importance. The Communists and other discontented elements will seek to harass the Castillo government, and may be able to place their men in a few minor government and labor union posts, and in educational institutions. However, under either Castillo or any likely successor government, we believe that the Communists will not succeed in securing positions prerequisite to a climb to power. (Paras. 31, 34)

7. We believe that if Castillo survives his immediate economic and political difficulties, with continued US support he will have a better than even chance of governing for the next few years. He will probably continue to adhere to a moderate course, and may be able to establish the basis for responsible constitutional government. (Paras. 63-64)

8. If the Castillo government should be overthrown, Guatemala would probably experience a protracted period of political instability. Rightist elements are more likely to be able to achieve this overthrow than any other group. (Para. 65)

## DISCUSSION

### I. INTRODUCTION

9. *The land and the people.* Guatemala is a predominantly agricultural country about equal in area to the state of Tennessee, with a population currently estimated at roughly 3,200,000. Most of the population is concentrated in the temperate highlands. The little-developed tropical land of the Pacific coast is sparsely peopled, and the northern half of the country — the densely forested Peten — is virtually uninhabited. About 70 percent of the Guatemalans are illiterate, the bulk of them Indians who constitute over half the population and who have relatively

little contact with the money economy. Almost 70 percent of the people reside in rural areas and over 75 percent of the labor force are agricultural workers.

10. The country displays most of the standard characteristics of underdevelopment: a low level of per capita production; inadequate transportation, power generation, and provision for health and education; a shortage of skilled labor and of transferable savings; and an inefficient and cumbersome public administration. Moreover, Guatemala's financial status depends to a great degree on revenue derived from the export of a single commodity — coffee. Efforts to diversify the economy

have been hampered by the shortage of investment funds for the requisite expansion of transportation and power facilities. In addition, the domestic market is small, because of low per capita production and high concentration of income. According to the country's 1950 census of agriculture, three-tenths of one percent of the landholders held over 50 percent of the total agricultural area. These are primarily the great coffee plantation owners (*finqueros*), who frequently invest their profits abroad rather than in the development of the local economy. During the Arevalo and Arbenz regimes the gap between the very rich and the very poor was not narrowed.

11. There are probably not over 200,000 Guatemalans who are more than marginally politically conscious. Of this group, the large landholders have almost never taken a role in the administration of the country other than to exercise powerful pressures toward conservatism. Only in recent years has the growing but still very small urban middle class begun to acquire a voice in the determination of affairs. As a result, the professional class retains a disproportionate influence in the operation of the government.

12. Many Guatemalans are passionately attached to the democratic-nationalist ideals of the 1944 revolution which overthrew the Ubico dictatorship. However, few understand the processes and responsibilities of democracy. Guatemalan politicians are disposed to indulge in intrigue against the government in power rather than to rely upon normal democratic processes to achieve their objectives. Hence there is an atmosphere of political unreality, characterized by individual manipulation and suspicion. At present many Guatemalans appear to be primarily concerned with preventing dictatorship of the right or of the left. A keen sense of nationalism, at times verging upon the irrational, colors Guatemalan politics. There is a strong tendency to attribute Guatemala's backwardness to foreign investors, especially those from the US. Even the most pro-US elements in the area are not immune to this type of extreme nationalism.

13. Responsible democratic government is therefore difficult to achieve. The country's most capable propertied citizens traditionally are unwilling to put themselves in jeopardy by participating in an administration which might fall overnight. Many of the Guatemalans formerly associated with the Arbenz regime and hence experienced in government are no longer available. Thus, the present government must rely in large part on youths with little background or aptitude for administration, or on men who served under Ubico. Furthermore, the absence of agreed political party programs and even of agreement on objectives greatly hampers efficient government.

14. Carlos CASTILLO Armas must reckon with the heritage of the revolution of 1944 and with the social and economic programs initiated by the Arevalo and Arbenz regimes. Although these regimes failed to establish a tradition of sound government or to improve, notably, the material well-being of large segments of the population, they nevertheless effectively popularized many of the tenets of the 1944 revolution. Castillo recognizes the political reality of the revolution and has accepted, in principle, most of the major reforms advocated by his predecessors. He has committed himself to the restoration of democratic forms and practices, to land reform, to the development of a modern economy, and to the protection of a free labor movement and other social gains. He is also guided by nationalism, among the more dramatic symbols of which are the Atlantic Highway and a new Caribbean port, both of which were initiated to break the monopoly of foreign enterprise.

15. During the Arbenz regime, the social and economic needs of labor and the peasantry were articulated and exploited by the small Communist leadership. Having infiltrated key administrative positions the Communists were able to promote measures which appeared to meet some of the aspirations of these groups. The Communists made considerable progress in the organization of urban and rural unions and were a prime influence in inducing the government to expropriate large

tracts of land for distribution among the landless. Agrarian reform affected at least 35,000 peasant families.

16. *Events of the past year.* The Arbenz regime collapsed in June 1954. After ten days of indecisive fighting between government forces and Castillo's small irregular "Army of Liberation," top army leaders turned against the regime. Although army leaders generally supported Arbenz because of the many benefits received from him, they became increasingly concerned at his tolerance of Communists in the government. As a consequence, the army's loyalty to Arbenz was weakened. Lacking the will to fight and realizing that Castillo would succeed, top army leaders forced Arbenz to resign. They formed a Junta, headed by Colonel Elfego MONZON Aguirre, which effected a cease-fire with the Liberation forces.

17. The present government evolved from an agreement reached on 2 July at San Salvador between Castillo and Colonel Monzon. This agreement was brought about after mediation by El Salvador and the US. The principal provisions of the agreement were to unite the national army and the armed forces of the Liberation, and to reorganize the Junta. Soon afterward the Junta was reduced to three men — Castillo, Col. Monzon, and Major Enrique OLIVA Quintana, an adherent of Castillo's. Castillo was named its president. One of the first steps of the Junta was an attempt to rid the country of Arbenz supporters. It immediately decreed the abolition of political parties. It established a "Committee of National Defense against Communism" (CDNCC) late in July. In the meantime most of the key Communist leaders had fled. The Junta also initiated an extensive investigation and punitive shake-up of the Communist-controlled labor movement, and issued an "agrarian statute" pending formulation of a new Agrarian Reform Law. In the reorganization of the armed forces, officers believed to be loyal to Castillo were given most of the high posts.

18. Shortly after these initial steps, dissension between the regular army and the Liberation forces broke out on 2-3 August following

an attack by the military academy cadets on Liberation forces in the capital. A large proportion of one regiment, led by disgruntled regular officers, supported the cadets. This action, which nearly resulted in a coup, was ended by the Junta's show of strength, in which the loyalty of Monzon and of the air force were decisive factors. After several weeks of declining public confidence in the regime, Monzon and Oliva voluntarily resigned to give sole power to Castillo as Provisional President of the Republic.

19. Elections were held in October, resulting in popular confirmation of Castillo and the seating of 60 official "National Anti-Communist Front" (FAN) candidates in the 66-seat Constituent Assembly. On 6 November Castillo was inaugurated for a term lasting until March 1960. He thus exchanged his *de facto* status for that of duly designated chief of state. Castillo continues to govern by decree on the basis of the "Political Statute" issued by the Junta in August 1954. The Assembly has virtually no legislative powers, and its primary function has been to draft a new constitution to replace that which was voided by the revolution.

20. Strife between regular and Liberation army officers again erupted in January 1955 when the government announced discovery of a "pseudo-Communist plot" involving dissident regular army officers. The government took strong and summary action to suppress the alleged plot. Six officers and men were summarily executed, several leading regular officers including Col. Monzon were banished, and additional Liberation officers were appointed to key military positions. In taking these actions, Castillo temporarily acceded to the persistent pressure of the Liberation elements for a through clean-up of potential dissidents. The January action was followed by two months of relative political tranquility, but subsequently the recurrence of rumors of plots and counterplots suggested growing dissatisfaction with the government.

21. The most immediate of Castillo's difficulties since last January have been economic. The problems of depressed business levels, un-

employment, and financial stringency inherited from the Arbenz regime had not been surmounted when the price of coffee fell sharply in mid-February 1955. The *finqueros* slowed down delivery of their coffee crops, which resulted in a continued lag in the collection of government revenue and a withholding of some millions of dollars from the economy. An equally important source of discontent has been the delay in the advent of the rainy season and in particular its destructive effect on corn, the staple diet of Guatemala. Some farmers have lost as many as three plantings, and there are indications that the corn shortage may extend into 1956. The US is providing 30,000 tons of corn and a small amount has been imported from Mexico. However, increased imports of corn are likely to be required during the remainder of the year.

22. Castillo's difficulties have been further complicated by poor management, and by the impatience of the articulate sector of the electorate for a return to constitutional government. The committee drafting the constitution has submitted the document to the Constituent Assembly. The committee's task has been made particularly difficult by the interjection of the religious issue. The Catholic Church — disestablished since 1871 — has sought to: (a) recover the right to own property; (b) re-establish monastic orders; (c) become active in the labor field; (d) open the public schools to religious education; and (e) win constitutional recognition of its "pre-eminence." After extensive acrimonious debate and political maneuvers, all but the last of these major demands of the Archbishop have been incorporated into the draft constitution. However, the religious issue is far from closed, and it is likely to prove a source of political dissension in the coming months.

## II. POLITICAL DEVELOPMENTS

### Position of the Castillo Regime

23. The ability of the present government to remain in power in the face of these difficulties probably results largely from: (a) US interest and support; (b) the substantial residue of personal popularity possessed by Cas-

tillo; and (c) the continued support of the armed forces. Most politically conscious Guatemalans believe that the US planned and underwrote the 1954 revolution, and therefore has a continuing responsibility for the success or failure of the present government. Castillo might have been deposed on any one of several occasions had his prospective opponents believed that the US would not give him prompt support. Thus, most criticism of the policies and performance of his government has been directed at his advisors and at the US rather than at Castillo himself.

24. One of Castillo's outstanding assets in the eyes of his countrymen is his sincere patriotism. Combined with that quality are modesty, informality, and accessibility. Castillo's moderation in employing the sweeping powers entrusted to him has reassured Guatemalans that he would not become a dictator. However, Castillo is inexperienced in government and lacks the intellectual qualities to overcome this deficiency with ease. Castillo often listens uncritically to anyone offering facile solutions to administrative problems. In dealing with his colleagues and subordinates his conspiratorial background has often caused him to vacillate between intense suspicion and unreasoning trust. He also suffers from frequent spells of nervousness and indecision.

25. Castillo has attempted to follow a middle-of-the-road course and to place national interests ahead of the interests of specific groups. He has identified himself with the more moderate aspects of the revolution of 1944 and with the struggle against Communism, corruption, and political oppression. However, the moderate political elements which support him have not been organized, and the individuals who immediately surround him in advisory positions are, for the most part, conservatively oriented. The majority of his Liberation army supporters advocate stronger and more extreme rightist policies, and the elimination from office of those who served the previous regime. On the other hand, some of his Liberation colleagues and many of the regular army officers advocate the more liberal principles of the revolution of 1944. Both groups, however, are divided

internally by personal ambitions and conflicting views. The Church-State issue further complicates the problem of formulating policies which could secure majority support. Castillo's government contains fervent anti-clericals as well as advocates of the Church, many of them far more intransigent than the relatively moderate Archbishop.

26. Lacking organized political support, Castillo has been unable fully to implement his program. The coalition of "Anti-Communist" groups (FAN) formed for the elections disintegrated shortly thereafter under the stress of conflicting aims and motives. Moreover, there has been little administrative talent to draw upon. Personnel appointed to administrative positions have been either inexperienced in government administration, interested primarily in jockeying for position in the present scramble to form political parties, or merely out to line their own pockets. Policy accordingly has vacillated, and its execution has been slow and indecisive.

### The Role of the Armed Forces

27. The army, which also commands the air force, continues to be essential to the survival of any Guatemalan regime. Addition of the Liberation elements has brought army strength to about 8,000 men. The air force consists of approximately 350 men and 44 aircraft of all types, of which the most important element is six F-51's obtained from the US. The National Police Force of 3,900 men is staffed by army officers. As long as the armed forces remain united and loyal, they are capable of maintaining internal security and of repelling attack from any of Guatemala's Central American neighbors.

28. The army traditionally is interested primarily in the defense and expansion of its prerogatives. Satisfaction of the army has usually been given top political priority by any Guatemalan regime. Castillo, however, has had the additional problem of restraining the rivalry between regular officers who served the previous regime and those of the Liberation. Resisting his Liberation supporters' demands for a complete purge, Castillo has moved cau-

tiously but steadily toward putting his trusted adherents in key positions. Colonel J. Ernesto NIEDERHEITMANN, an important Liberation commander, is now army chief of staff, and the only remaining highly placed holdover from the Arbenz regime is Colonel Enrique CLOSE de Leon, the defense minister. Castillo is under pressure to replace the latter, but he is probably deterred both by Close's considerable prestige and following in the army, and by a desire to offset overwhelming Liberation influence.

29. Many of the regular elements of the army probably remain somewhat dissatisfied with their position under Castillo. However, since their leaders have largely been replaced by prominent Liberation figures, there is little likelihood of disgruntled regulars initiating an organized rising against the present regime. In the unlikely event that any of the more popular exiled army leaders were to launch a rebellion, a small portion of the army would probably try to join and some would wait on the sidelines. However, the bulk of the army would probably remain loyal to Castillo and would be able to cope with the situation unless Castillo's political position had seriously deteriorated and the rebellion were conducted on a substantial scale. If rightist extremists among the Liberation elements in the army were to attempt a coup, it would probably be put down by the integrated regular and Liberation forces.

30. Castillo probably will continue to strengthen his position by placing his trusted supporters in key army positions and by making further efforts to satisfy the army's material demands. His position vis-a-vis the armed forces will be further strengthened by the recently signed Mutual Defense Assistance Pact with the US. Nevertheless, we believe that there will continue to be sporadic unsuccessful attempts against the government.

### The Potential Opposition

31. *The Communist threat.* Communist and Arbencista subversive activity — both domestic and foreign — has not been a serious threat to the political stability of the

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Castillo government. There were almost certainly no more than 4,000, and perhaps substantially fewer, Communists in Guatemala at the height of Arbenz's power. The most prominent figures of the former regime are no longer in Guatemala, but probably about half the Communists, and a much larger number of Arbenz sympathizers are still in the country. Communist subversive activity since July 1954 has been largely confined to the circulation of sporadically produced mimeographed propaganda, and some broadcasts over clandestine radio stations may have been Communist-inspired. However, the organization, *Frente de Recuperacion Nacional*, may serve as cover for the remnants of the Communist Party, reconstituted as an underground movement.

32. Communists and Arbenzistas in exile do not constitute an immediate threat to the Guatemalan government. The exiles are presently resident in several Latin American countries, with the largest concentrations in Mexico, Argentina, Brazil, El Salvador, and Ecuador. Potentially the most dangerous group, which includes the majority of the key figures in the former regime, is in Mexico. These exiles have received assistance from Mexican Communist and pro-Communist groups and probably have attempted to form a political organization. However, this activity apparently is impeded by divisions between Communists and Arbenzistas and by splits within each of these groups. The exiles in El Salvador are fewer in number, but are potentially important by reason of their proximity to Guatemala.

33. The government has given the principal responsibility for investigating Communists to an agency known as the Committee of National Defense against Communism (CDNCC). The CDNCC, which has the power to arrest, has often proven incompetent, overzealous, and arbitrary and has aroused public disapproval and even ridicule. There are strong pressures for its dissolution. In response to these and other pressures, Castillo probably will soon reorganize the government security system.

34. We believe that the Communist and Arbenzista threat at least in the short term will remain of relatively little importance. Despite the administration's scrutiny, the Communists may be able to place their men in a few minor government and labor union posts, and in educational institutions. There are many restless and discontented Guatemalan groups which might become vulnerable targets in a deteriorating economic and political environment. These include unemployed workers, peasants threatened with eviction from their lands, disillusioned student and intellectual elements, and discharged government employees. The Communists and other discontented elements will seek to harass the Castillo government. However, under either Castillo or any likely successor government, we believe the Communists will not succeed in securing positions prerequisite to a climb to power.

35. *Labor and rural groups.* Guatemalan labor was the class most adversely affected by the overthrow of Arbenz. The organization of the labor movement was virtually destroyed after the revolution. After being favored for a decade, the workers are now often the object of official suspicion, and are waging an uphill battle to reconstitute their trade unions. Moreover, depressed business conditions since the revolution, as well as efforts by employers to negate the benefits granted to labor by the previous regime, have increased unemployment and intensified labor's feelings of insecurity and resentment. Although Castillo made some promises to labor, he has been unable to redeem them fully because of economic difficulties and conservative opposition. The result has been a decline in Castillo's popularity and an increase in restlessness among those groups.

36. In recent months the government has shown greater interest in safeguarding trade union liberties. By mid-1955 twenty-six trade unions, including the half dozen most important ones, had already been legally established and others were awaiting approval. More forceful attempts are being made to implement the Labor Code, and the Labor Courts, which immediately after the revolu-

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tion had dealt harshly with workers' claims, are now ruling more favorably to labor. On balance, labor leaders appear to feel, that despite antilabor sentiment in certain politically influential circles, Castillo offers the best present hope for the reconstitution of a free labor movement.

37. In the eyes of labor the test of Castillo's sincerity in labor matters will lie in his willingness to permit the establishment of a strong central labor organization free of political control. To date, two central organizations have been established in embryonic form. *The Federacion Autonoma Sindical (FAS)*, which represents the bid of the Catholic Church for labor support, has so far failed to attract an important segment of labor because of anticlerical sentiment among workers and the political ties of its leader with the Administration. The *Consejo Sindical de Guatemala (CSG)* represents a small group of relatively well established trade unions which are moderate in outlook and have a promising leadership. If Castillo accedes to the CSG's request for legal recognition free of political control, he will probably win labor's support at least for the near future. We believe there is a better than even chance that Castillo will attempt to comply with the CSG's wishes.

38. Rural groups are having even more difficulty in obtaining favorable government action. The Arbenz regime resettled rural workers on government lands as well as on those it acquired through expropriation. It also fostered the organization of plantation workers. Although many of the benefits given the peasants were illusory, and peasant organizations were mainly used by the Communists for political purposes, the Arbenz regime's action responded to genuine rural demand and need for land reform. Castillo is under strong pressure from the landholders to restore expropriated properties and to continue to deny rural workers the right to organize. In most cases he has postponed the return of land to original owners. He is developing a plan which envisages the resettlement of 5,000 peasant families annually on public lands in the Pacific Coast region. With US

technical and financial help, this project over the long run is likely to prove of substantial assistance in quieting rural discontent. In fact, the government probably will have more to fear over at least the short term from the conservative critics of agrarian reform than from the disorganized and virtually leaderless rural population. On the other hand, the possibility of sporadic violence among plantation workers cannot be excluded in the event of critically worsened economic conditions against which the government fails to take prompt remedial action.

39. *The threat from the Right.* The extreme rightists among Castillo's supporters, together with influential conservative civilian elements throughout the country, probably constitute the chief potential source of opposition to the government. Most of these conservative factions strongly criticize Castillo for his "soft" policy toward both civilian and military officeholders of the previous regime, for his moderate policies toward labor and agrarian problems, and generally for his refusal to turn back the clock to 1943. However, Castillo so far has kept rightist discontent within bounds. There is no indication that the diverse rightist elements are preparing any concerted attack on the government. A rightist coup would be highly unlikely so long as Castillo retains US support and that of the Guatemalan armed forces, and can secure public confidence by making some progress toward solving Guatemala's economic problems.

40. The personalities around which conservative opposition might crystallize are few. Juan CORDOVA Cerna, former head of the National Council for Economic Planning and the foremost civilian participant in the Liberation, has intermittently clashed with Castillo. Staunchly conservative and highly ambitious, Cordova has persistently been cited as Castillo's greatest rival. However, Cordova's power appears to have been neutralized. Shortly after the revolution the return to Guatemala of General Miguel YDIGORAS Fuentes, a former presidential aspirant, posed another problem. Castillo at least temporarily has resolved this problem by assigning Ydigoras to the post of Minister to Colombia.

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Finally, Chief of Staff Col. Niederheitmann, although currently a close associate of Castillo, is the type of conservative military "strong man" around whom disaffected rightist elements might naturally rally.

### Short-Term Political Prospects (Through Early 1956)

41. The remaining months of this year and those of early 1956 will be especially difficult for Castillo Armas. The draft constitution has been submitted to the Constituent Assembly for approval by fall. If it is adopted, the Constituent Assembly is to schedule elections for a new Congress, probably for some time in the winter of 1955-1956. Meanwhile, in preparation for a resumption of normal political activities, the formation of political parties has begun. In addition, the government will have to cope with budgetary and other economic difficulties created by depressed coffee prices and by the inadequate rainfall. The ability of the present government to survive will probably be determined by the effectiveness with which Castillo deals with these problems, by the amount of US assistance, and by the international coffee market situation.

42. Much will also depend upon Castillo's success in creating a political organization which will give his government adequate support. Such an undertaking is rendered difficult by the widely conflicting views and interests of even his staunchest adherents. Nevertheless, the process is underway. The administration has launched an "official" political party named the National Democratic Movement (MDN). The MDN's middle-of-the-road policy statement is signed by 144 individuals representing all shades of non-Communist political beliefs. The government's strongest supporting organization to date, the Committee of Anti-Communist University Students (CEUA), has dissolved itself and has joined the MDN. The old Liberal Party, reconstituted as the National Democratic Association (ANDE), has decided not to join the new party. The hybrid character of the MDN is already the target of considerable criticism, and it is improbable that such diverse elements

can be held together within a single party. If the MDN splinters or does not attain a dominant position, Castillo probably will have to attempt to form a coalition of parties willing to support his government. In either case Castillo will have difficulties in securing sustained and consistent legislative and political support for his moderate policies.

43. To maintain control and to carry out an effective program in the period ahead will require a substantial degree of skill on Castillo's part. Castillo has shown some talent in the past for playing off the extremes against each other. On balance, we believe that if economic conditions do not further deteriorate, Castillo will probably be able to retain office both during and immediately after the period of reconstructing constitutional government.

### III. ECONOMIC DEVELOPMENTS

44. *Characteristics of the economy.* The economy of Guatemala is based primarily on the production and export of coffee. Coffee production amounts to over 1.2 million quintals<sup>2</sup> annually, with most of it going into the export trade. Government-owned lands — largely expropriated from the Germans during World War II — accounted for about one-third of that production at the time of their nationalization. Coffee accounted for 79 percent of total exports, which were valued at about \$96 million<sup>3</sup> in 1954. It is the most important single source of Guatemala's revenues; in recent years coffee export taxes have constituted around 20 percent of all government revenues. Moreover, since the major direct tax is on business profits, and since domestic prosperity depends mainly on the coffee trade, a drop in world coffee prices has a multiple deteriorating effect on government revenue.

45. Bananas, the only other major export crop, have averaged roughly 10 percent of the value of exports over the past several years. Chicle, lumber, and essential oils are the remaining exports of any significance. How-

<sup>2</sup> One quintal = 100 Spanish lbs. = 101.4 English lbs.

<sup>3</sup> The Guatemalan quetzal is freely convertible and has been at par with the US dollar since 1924.

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ever, Guatemala produces a good grade of long-staple cotton, and increasing production may result in a surplus for export this year. There are indications of commercially exploitable oil deposits in the northeastern part of the country, and the Castillo government has prepared a Petroleum Law which it hopes will attract foreign investment while appeasing nationalistic fears of foreign exploitation. Industry in Guatemala is confined largely to the processing of agricultural products and the manufacture of simple consumer goods and building materials. Even such industry depends heavily on imported capital goods, equipment, and raw materials. Power facilities barely meet present requirements.

46. In 1954, Guatemala's GNP is estimated to have been approximately \$650 million. While GNP in real terms (constant prices) appears to have been growing at about three percent per year over the period 1950-1954, per capita income changed very little owing to the rapid rate of population growth, estimated at two and a half percent a year. From year to year Guatemala's GNP is subject to wide fluctuations reflecting abrupt changes in the terms of trade which, in turn, are governed largely by the trend of coffee prices. Average saving and investment are relatively low, as in virtually all underdeveloped countries, and are subject to the same short-term fluctuations as the GNP.

47. The book value of direct US investments in Guatemala was \$107 million in 1953, almost all represented by the branches and subsidiaries of three US corporations: the United Fruit Company (UFCo); International Railways of Central America (IRCA); and Empresa Electrica, a subsidiary of American and Foreign Power.

48. UFCo controls most of the production and export of bananas in Guatemala. The company operates two divisions: the Atlantic, with its main office at Bananera; and the Pacific, with headquarters at Tiquisate. The symbol of foreign exploitation in Guatemala, UFCo was consistently attacked by the Arbenz regime, which expropriated almost 420,000 unused acres of its total land holdings of about 560,000 acres. UFCo has achieved good rela-

tions with the Castillo government. In two contracts UFCo regained about 245,000 acres expropriated from its Pacific division, and agreed to pay taxes on that division's net profits up to a maximum of 30 percent. It also ceded to the government without charge about 110,000 of those acres. A contract covering the Atlantic division remains to be negotiated. However, despite UFCo's improved relationship with the government, and the company's relatively high wage and living standards, it faces a strong residue of hostility in Guatemala. Castillo may have to refrain from making new agreements with UFCo for a time. On the other hand, UFCo has stated its intention of making large new investments in Guatemala after settlement of the US anti-trust suit now pending.

49. The US-owned IRCA operates virtually all of Guatemala's roughly 700 miles of track. It carries most of the country's freight and affords the only means of access by land to the major Caribbean port, Puerto Barrios. UFCo has a 43 percent interest in the IRCA system, which is linked with the fruit company's plantations, and obtains an artificially low freight rate for its bananas. At the same time, IRCA subjects other freight to excessively high charges. As a result, Guatemalans are strongly critical of IRCA and are most anxious for the completion of the Atlantic Highway which will break the railroad's monopoly of land traffic to the Caribbean.

50. Empresa Electrica provides roughly 75 percent of Guatemala's power, and the government controls the remainder. Over two-thirds of the power is derived from hydro stations. Resources are centered around the capital and are only sufficient to provide for the cities and the larger towns. Empresa Electrica proposes to expand its generating capacity through the investment of about \$17 million over a ten-year period. However, its plan has not yet been approved by the government, which objects to certain features and considers the company too conservative. Furthermore, in indicating its displeasure with Empresa Electrica, the government has intimated that it might attempt to carry out a power expansion program itself.

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51. *Government economic policies.* The economic policies of the Arbenz regime probably retarded economic growth and led to a substantial increase in the public debt. Moreover, the Guatemalan economy weakened considerably following the fall of Arbenz. Despite the aid received from the US the economy has not fully recovered, largely because of unfavorable weather and the drop in world coffee prices. The government has followed conservative fiscal policies and will probably achieve a balanced budget for FY 1956. However, budget revenues and expenditures for FY 1956 are estimated at around \$66 million (excluding US aid), compared with last year's approximately \$73 million (including the special Liberation tax) and, more important, with the roughly \$75 million expended by the Arbenz government during its last year in office.

52. The government has made a number of mistakes in its economic policy. The abrupt halting of public works projects helped to swell the unemployment figure to perhaps as high as 30,000. The government has vacillated in its attitude toward encouraging private investment, it has not instilled sufficient business confidence to insure sustained expansion of the private sector of the economy, and it has failed to make funds available for large public investment.

53. An extensive highway construction program offers the Castillo regime an effective means of coping with both its immediate and long-range economic problems. With only a few hundred miles of paved roads out of a total of roughly 6,000 miles, the transportation net is wholly insufficient for the economic needs and development of the country. Of the \$6,425,000 US aid for FY 1955 (excluding emergency corn shipments) the bulk has been devoted to the road-building program, with Guatemala contributing about half as much as the US. The main effort is on the Inter-American Highway and on improving a highway, paralleling the Pacific coast, which traverses the richest agricultural area in Guatemala. Work on the final quarter of the all-weather Atlantic Highway to Santo Tomas will begin as soon as funds can be made available. The Castillo administration has applied

to the IBRD for a \$20 million loan to finance local costs of highway construction, as well as for various development projects requiring agricultural machinery and for industrial plants.

54. *Economic prospects.* The Castillo government faces acute short-range economic problems. The most serious of these is the failure of the corn crop. The ability of the Castillo regime to meet this crisis will depend largely on the promptness and adequacy of US assistance. Serious dislocations in the rural economy not only would have a depressing effect on the entire economy, but would increase public dissatisfaction with the regime. Another serious problem is unemployment. However, we believe that the present level of unemployment will not confront the Castillo regime with insuperable difficulties during the summer months. With the end of the rainy season in late fall, unemployment probably will be reduced by increased activity on the highway projects and an expansion of the public works program. If Castillo makes substantial progress with these problems, and impresses political elements with the effectiveness of his leadership, a rise in business confidence and activity is likely to result.

55. Over the longer haul, substantial economic improvement will depend on an expansion of capital investments, public and private, including development of the Pacific coastal area. The present volume of private investment cannot readily be assessed, and there is no concrete evidence of any large-scale repatriation of capital. On the other hand, Guatemala's reserves of gold and foreign exchange have been steadily rising and now stand at a new record figure of about \$57 million, possibly indicating some repatriation of capital. In 1953, when coffee prices were roughly equal to the present levels, private investment was estimated at about \$39 million. Once the public works program gets fully underway and if coffee prices remain stable, business confidence will probably improve sufficiently to insure a level of domestic capital investment at least equal to that of 1953. Moreover, assuming that the IBRD loan is granted, that the government consequently will not have to finance highway construction in FY 1956, and

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that the cost of government operations will remain approximately constant, the Castillo regime probably will be able to maintain public investment next year at close to the 1953 rate of \$29 million.

56. On the other hand, there will almost certainly be a gradual expansion of government expenditures over the next several years as land reform measures are adopted, expropriation claims are settled, and public health, education, and other social services make greater claims on the treasury. In these circumstances, a considerable revision of the tax structure will be required if government deficits are to be avoided. The Castillo government has drawn on US technical assistance funds to employ American consultants to revamp thoroughly both the tax laws and customs tariffs with a view toward increasing government revenue. A program for Guatemala's first income tax is also being readied, and there are indications that it will be accepted, though with resignation, even by the professional class so long as the rates are kept as moderate as is now envisaged.

57. Completion of the new Pacific highway will probably result in development of the Pacific coastal land and constitute one of the most promising aspects of Guatemala's future. Already expanding coffee production probably will accelerate, even in a period of low prices, if there are stable political conditions, and if world demand remains at approximately present levels. There is also at least an even chance that oil will be exploited in profitable quantities, and that the Lake Izabal area will yield increased exports of lumber and wood products.

#### IV. INTERNATIONAL RELATIONS

58. The principal objectives of Guatemala's foreign relations under Castillo are: (a) closer ties with the US; (b) improved relations with immediate neighbors; and (c) the end of the country's isolation in hemispheric affairs.

59. The Castillo administration has been consistently pro-US in its policies and attitudes, seeking advice and assistance on many domestic problems and cooperating closely on

international questions. In fact, Castillo may have damaged his potential capacity for leadership by excessive reliance on US advice and aid. At the same time, Castillo and, to a greater degree, his associates on occasion suspect the motives of representatives of the US. Nevertheless, Castillo's friendship for and reliance on the US is the most stable element in Guatemala's foreign affairs.

60. Guatemala's relations with its neighbors have greatly improved under Castillo, largely because of the moderate character of his administration and the cessation of Guatemalan Communist propaganda activities in those countries. At Castillo's request, Guatemala was readmitted to the Organization of Central American States (ODECA) and is to play host at its scheduled summer meeting. Furthermore, Guatemala has completed, or is negotiating, commercial treaties with Costa Rica, Honduras, Nicaragua, and El Salvador. Potential friction exists, however, between Guatemala and its neighbors because of ideological and personality conflicts. Castillo reportedly distrusts Osorio of El Salvador, although to date their official relations have not been unfriendly. His suspicious attitude toward Figueres of Costa Rica is owing partly to ideological differences and partly to the latter's noncommittal position during the 1954 Liberation. On the other hand, Castillo has friendly ties with Somoza of Nicaragua and PEREZ Jimenez of Venezuela. In any case, because of his domestic problems, his ties with the US, and his moderate nature, Castillo is unlikely to meddle actively in Central American politics unless a clearly unfriendly government comes to power in a bordering state.

61. Mexican-Guatemalan relations were strained in 1954 as a result of Mexico's position as sanctuary for the majority of Guatemalan Communist and Arbencista leaders. However, Mexican authorities recently have imposed close surveillance over the important Guatemalan exiles and have prohibited their political activities. The conclusion of a trade agreement for importing Mexican corn, the informal visit of ex-President Aleman to Castillo, and the appointment of a top-ranking Mexi-

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can ambassador to Guatemala have contributed to improved relations between the two countries.

62. The Castillo government has also taken steps to re-establish Guatemala's prestige in hemispheric affairs by rejoining ODECA, adhering to the Caracas Resolution, and depositing its ratification of the OAS Charter and the Rio Treaty. On the other hand, the Castillo administration has reaffirmed Guatemala's traditional claim to British Honduras. Reservations to this effect have been appended to Guatemala's ratification of both the Rio Treaty and the OAS Charter. Despite the emotional strength of this issue, however, it is unlikely to prove a source of serious friction in the area during the foreseeable future.

#### V. PROSPECTS FOR STABILITY IN GUATEMALA

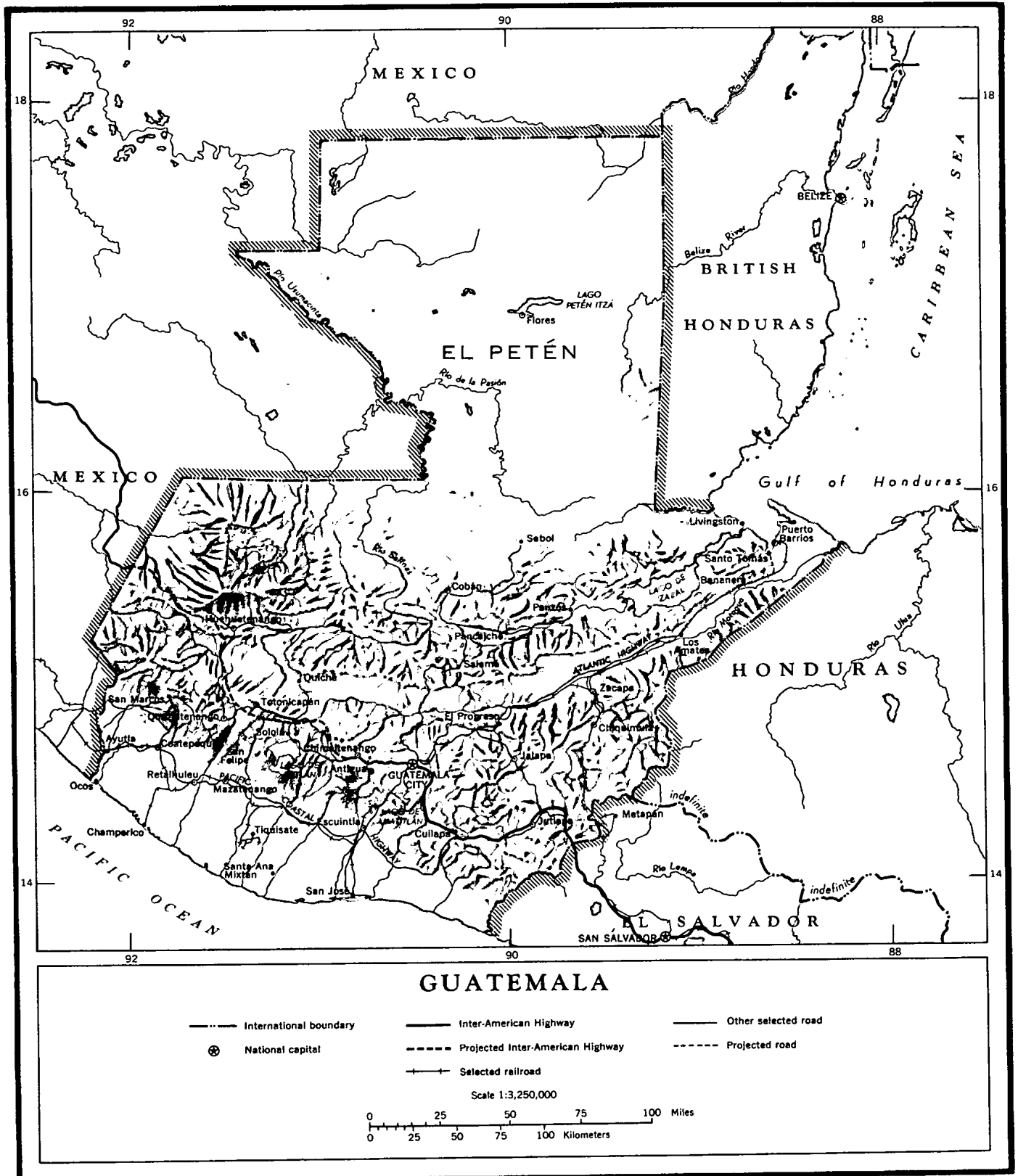
63. We believe that if Castillo survives his immediate economic and political difficulties,

with continued US support he will have a better than even chance of governing for the next few years.

64. Castillo probably will resist extremist pressures and continue to adhere to the moderate course he has followed to date. If he maintains his prestige as a mediator, he will probably be able to retain much of his present authority even in the face of an unruly legislature. He may also be able to make further progress in unifying the armed forces behind him. Thus, Castillo may be able to remain in office long enough to establish the basis for responsible constitutional government.

65. On the other hand, if the Castillo government should be overthrown, Guatemala would probably experience a protracted period of political instability. Rightist elements are more likely to be able to achieve this overthrow than any other group.

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