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ACTION Per Dept. Use Only	ARR-4	DEPT.	ARMY-2	REP-2	*IRC-3	*E-4	CA-10
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SUBJECT: Foreign Investments:- São Paulo: Krupp Expanding Brazilian Operations  
ARMY-4 TAR-2 IN-7 AG-3  
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SUMMARY

Toward the end of 1956, with the arrival of several directors and engineers of the German Krupp organization, a program for the expansion of Krupp's Brazilian operations was initiated. At that time, high-level discussions were held regarding the possibility of Krupp entering the heavy-duty equipment manufacturing field with the production in Brazil of locomotives and heavy-duty trucks.

Early negotiations were largely confidential. It was not until September 25, 1957, when the three top directors of Frederick Krupp A.G.'s Brazilian subsidiary asked São Paulo State Governor Janio Quadros for assistance, that the "Krupp case" became a casus celeberrimus providing a political and economic controversy that has not yet been resolved. This controversy must be considered as part of growing agitation on the part of São Paulo industrial and political circles to publicize a business slowdown and alleged recent discriminatory economic decisions made by the Federal Government (see ConSex Despatch 150). The directors of Krupp requested the governor to use his influence to iron out certain difficulties which were being encountered by the company in attempting to expand its operations. The local press reported that at this meeting the Krupp representatives had stated that the Federal Government appointed commissions were withholding permission for the firm to import machinery under SUMOC's Instruction 113.

Before these statements could be verified, the Krupp case became São Paulo headline material and raised the ire of already touchy Paulistas. In rapid succession (1) the Juandai Municipal Chamber approved a vote of censure against the Federal Government, (2) Santos and Campinas followed suit, (3) the São Paulo Assembly heatedly debated "the sabotage of Krupp," (4) São Paulo newspapers took up the attack in full force, announcing the possible withdrawal of Krupp from Brazil, and (5) upon appeal to the Juandai Commercial Association, the city's business and industrial activities came to a standstill on October 4 to protest the "attitude adopted by the Federal Government."

No sooner had these events occurred than the São Paulo press took up the hue and cry. Editorials blossomed, hitting at the "Federal Government's discrimination against São Paulo" and calling for "defense measures."

The Federal Government, stung by the criticisms, arose to the defense. Federal Minister of Transport Lucio Meira declared that (1) the Federal Government had not

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rejected Krupp's projects. (2) Krupp had presented no detailed production program to the Federal Government. (3) the Government had not concluded studies with respect to the manufacture of locomotives, and (4) that Krupp's manufacturing program for heavy-duty trucks was still under study.

These strong statements by the Federal Government apparently had the desired effect. Within a matter of days the São Paulo press slackened its attacks, and several editorials defending the Federal Government's position suggested that perhaps Krupp had overplayed its hand.

The Krupp controversy can be largely laid to Paulista over-exuberance, growing evidence of a business slowdown, and growing controversy between the São Paulo business community and Federal Government economic policy.

The Federal Government quite clearly had valid reasons for carefully scrutinizing Krupp's broad and complicated expansion program. The Consulate General believed that some manufacturing plant at Campo Limpe near Jundiaí in the state of São Paulo will eventually be approved. Krupp's production of heavy transportation equipment, particularly heavy duty trucks, could have an unsettling effect on the future Brazilian truck market.

#### BACKGROUND

Although Krupp products were imported into Brazil as far back as 1898, it was only in October of 1952 that the German firm's local representatives, Importadora e Exportadora Brasileira MOT, S.A., were made a Krupp subsidiary and changed their name to Industria Nacional de Locomotivas (INL), Ltda., with an authorized capital of Cr\$10 million.

Krupp had shown an interest in manufacturing locomotives in Brazil as early as 1951 when it presented to the Brazilian Council for Economic Development a project for the construction of locomotives. For several reasons, including bureaucratic delay, inactivity on the part of Krupp, changes in the Federal and São Paulo State Governments, and the waning influence of the Council of Economic Development, the project was effectively shelved until 1956.

During that year two events occurred which gave new impetus to Krupp plans in Brazil. In the first instance, the São Paulo State Government became aware of the fact that Belo Horizonte in the state of Minas Gerais was Krupp's choice for the location of its new production facilities. It immediately made INL an advantageous offer to locate in São Paulo. It offered land and buildings with an estimated value of Cr\$21.5 million for only Cr\$12 million.<sup>1)</sup> The offer stipulated that in the event that Krupp was not manufacturing locomotives within a period of five years, the land and buildings would revert to the state and the Cr\$12 million would be returned. INL immediately accepted the offer, and the sale was duly registered on September 10, 1956.

<sup>1)</sup> The property, formerly belonging to the Coffee Institute, is at Campo Limpe near the city of Jundiaí and includes a siding of the Santos-Jundiaí railway.

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The second event which gave impetus to Krupp's new production program was President Kubitschek's visit to Germany in 1956. He visited the Krupp factory at Essen and informed Krupp's president, Mr. von Bohlen und Halback, that the company's plans in Brazil would probably receive the Federal Government's favorable consideration.

In November, 1956, Mr. von Bohlen und Halback visited Brazil, had important talks with President Kubitschek and Governor Quadros, and expressed the hope that the Company's expansion plans would now be given favorable consideration by the governments of Brazil and the State of São Paulo.

A revitalized Council for Economic Development, presided over by Federal Minister of Transport Inácio Meira, was appointed to study the use of diesel locomotives by the Brazilian Railways. On January 23, 1957, the Council received IHL's new project for the manufacture of Krupp locomotives in Brazil. In this locomotive program, for the first time, brief mention was made of the company's intent to also produce heavy-duty trucks. Toward the end of April, a detailed production program for the manufacture of 18-ton, heavy-duty trucks was presented to the Executive Group of the Automobile Industry (GEIA) for study and approval. It was particularly interesting to note that both programs detailed Krupp's capital position and plans for the future.

Brazil's Krupp subsidiary, originally capitalized at Cr\$10 million, increased capitalization to Cr\$30 million in 1956. Brazilian participation is concentrated in the following principal stockholders: The V. Veloso Borges group (a powerful textiles concern), the Cia. Tanbatê Industrial, the Banco Aliança de Rio de Janeiro (allied to Deutsch-Südamerikanische Bank of Hamburg), and Messrs. Rudolf Krauss and Schluchtmann (IHL's managing directors).

On July 23, 1957, a further report to the Council of Development indicated that Krupp intended to invest \$4 million and 17 million West marks in cash, as well as \$7 million and 28.5 million West marks in machinery and equipment. The sources<sup>2)</sup> for much of the information contained in this despatch have indicated to the reporting officer that the parent company had also declared itself willing to forego remittance of profits for an indefinite period, reinvesting in the Brazilian operation.

While the programs of Krupp are at present quite confusing, the president of the company did outline his company's projects to the press, and it can be safely assumed that these remain basically unchanged. If the program is approved by the Federal Government, IHL will begin with the production of 16 to 18-ton, heavy-duty trucks and the manufacture of steam, diesel, and/or electric locomotives. Initial output has been fixed at 50 units annually with production gradually increasing to an annual rate of 100 units by 1962. What is not generally known is the fact that the over-all Krupp program also foresees the manufacture of heavy-duty cranes, deck equipment, and mining machinery, as well as the construction of a cement factory. Associated plans foresee the production, with the firm of Heinrich Lanz of Mannheim, Germany, of bulldozers, tractors, and agricultural machinery.

<sup>2)</sup>Members of the local Krupp organization and the German Consulate General

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In view of the complexity of the company's program, it is understandable that the Federal Government has shown some reluctance to giving a blanket approval to Krupp's Brazilian expansion plans. Both the locomotive manufacturing program and the heavy-duty truck manufacturing program have recently been severely criticized by the Federal Government.

As regards the locomotive program, Transport Minister Lucio Meira has stated that IHL has not presented a detailed locomotive manufacturing program, but has only indicated "an intent to manufacture." He claims that this "intent" was presented to the Council for Development in a ten-page document which was, in his opinion, barely an outline of IHL's basic locomotive manufacturing program. The doctrine stated that by 1960, 70 percent of the locomotive's content by weight and 50 percent by value would be of national production. Minister Meira goes on to say that this document does not even specify what type of locomotive IHL intends to manufacture. He further stated that IHL claims that the company had made arrangements with General Electric to manufacture the locomotive's electrical equipment and with Cooper-Bessemer to produce the diesel engines. Minister Meira added that the Council for Development has ascertained that neither General Electric nor Cooper-Bessemer has signed any such agreement with either Krupp or IHL.

The Consulate General believes that perhaps what most irritated the Federal Government was a series of what Minister Meira called "demands" made by IHL directors. The two principal "demands," as best as can be ascertained, were that (1) the Federal Government should guarantee IHL a firm order for 250 locomotives based on an annual anticipated output of 50 units and that (2) the Federal Government should guarantee IHL priority in the supply of locomotives to the exclusion of competition. The Council for Development, in the reporting officer's opinion, would not and could not approve a locomotive manufacturing program dependent on these conditions. It has been ascertained that there is some doubt as to whether Brazil can absorb the proposed output. To be sure, some 165 locomotives were imported in 1967, and it is understood that 50 more units are on order with General Electric. These purchases, however, were in connection with a major railway overhaul and replacement program, and it is quite doubtful if in the future the Brazilian railway system could absorb 50 to 100 new locomotives annually.

In contrast with the locomotive program, the heavy-duty truck program presented by IHL to the GEIA is very detailed. It ignores, however, federal decree 39412 of June 16, 1966, which restricts axle weight to 8 tons. Krupp's trucks weigh in the neighborhood of 10.6 tons per axle. An interesting development along these lines, however, is that early in October President Kubitschek appointed a commission to study the pros and cons of manufacturing heavy-duty trucks in Brazil. This commission, which was composed of representatives of the National Highway Department, the National Council of Transportation, the Association of the Motor Vehicle Industry, and the GEIA, has now recommended the manufacture of trucks weighing up to 10 tons per axle. As Krupp's vehicles could readily conform to this axle weight, it is quite possible that if the recommendations are approved by President Kubitschek, GEIA will in turn approve Krupp's heavy-duty truck production plan.<sup>3)</sup>

<sup>3)</sup>Other programs for the manufacture of heavy-duty trucks presented to GEIA and not yet approved include Venag's Scania-Vabis, Mercedes' 16 tonner, Borgward's 18 tonner, International, and Res.

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Although the São Paulo press has toned down its attacks, resentment against what the Paulista calls "Federal discrimination against the state of São Paulo" is still strong. The bitterest attack against the Federal Government was perhaps the petition presented to the Juiz de Fora Municipal Chamber, which contended that President Kubitschek and self-interested political and industrial groups deliberately blocked the expansion of Krupp in the São Paulo area. The note also accuses President Kubitschek of championing his native state of Minas Gerais vis-à-vis São Paulo to the detriment of Brazil's over-all economic development.

The Santos and Campinas Municipal Chambers, backstepping the action taken by Juiz de Fora, sent telegrams to President Kubitschek, the Minister of Finance, the President of the Bank of Brazil, and the president of the Chamber of Deputies protesting "federal interference in São Paulo's industrial development." In the Federal Chamber of Deputies in Rio de Janeiro, São Paulo Federal Deputy Herbert Levy attacked what he called "the Federal Government's deliberate sabotage of Krupp's plans in São Paulo." The São Paulo Legislative Assembly itself held stormy debates, criticizing Federal Government policy. These debates were headlined by São Paulo papers.

#### COMMENT

The whole controversy, this office believes, has been highly exaggerated in the usual "Paulista spirit." Nevertheless, it is important to note that while the Federal Government normally welcomes responsible foreign capital, it is always wary of capital that tries in any way to influence, change, or to put pressure on the formulation of Brazilian economic policy. Fewer tactics and repeated threats to move to Argentina only served in this case to antagonize already touchy statesmen in Rio de Janeiro.

The natural tendency to play one foreign company against another was evident throughout the controversy. International General Electric Company, since the war Brazil's major supplier of electric and diesel locomotives, was often named as a powerful and somewhat sinister force behind the scenes. For two weeks there have been cautious press notices that another well-known foreign company is interested in manufacturing diesel and steam locomotives in Brazil. According to a recent statement from OELA itself, a French company (probably BERLIET) has also presented a program to produce heavy-duty trucks - "Its program will be duly studied and compared with Krupp's."

The reporting officer believes that while the over-all Krupp program centric confusing and unrealistic inconsistencies and was poorly presented at an unfair time, the Federal Government will eventually approve manufacture at Campo Limpo. Any national reporting on the motor vehicle industry cannot at this time completely discount Krupp as a probable important future supplier of heavy-duty trucks to the Brazilian market. While heavy-duty trucks are not part of the present Mercedes-Benz, General Motors, Ford, and Willys progressive manufacturing programs, Krupp will probably offer strong direct and indirect competition to these still fledgling undertakings.

*Richard P. Butrick*

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Consul General

cc to Rio *[Signature]*

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