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1 APR 1977

MEMORANDUM FOR: Mr. Robert Pastor
NSC Staff Member
Room 380
Executive Office Building

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Attached is a memorandum on the FRG-Brazilian nuclear accord developed by the Office of Regional and Political Analysis. This memorandum is a response to questions originally addressed to

Copies have also been sent to Ms. Tuchmann, Mr. Hunter, and Mr. Nye at the State Department.

/s/ Stansfield Turner

STANSFIELD TURNER
Admiral, U.S. Navy
Director, Central Intelligence Agency

Attachment:
RP-M-77-10073

Date

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CENTRAL INTELLIGENCE AGENCY
 Directorate of Intelligence
 April 4, 1977

INTELLIGENCE MEMORANDUMTHE FRG-BRAZIL NUCLEAR SALE:CHOICE AND CONSEQUENCES

West Germany and Brazil continue to react negatively to US efforts to persuade them to modify their 1975 nuclear accord. West Germany has indicated its determination by public statements made at the highest level to implement the nuclear accord with Brazil without substantial change. Brazil has rejected any modification of the contract to purchase reactors and sensitive facilities and has angrily denounced US attempts to block its plans.

US relations with both countries have already come under considerable strain over the nuclear accord. Prospects are that additional strains will result, no matter what the final resolution of the issue. To a great degree, strains in relations with Brazil and the FRG were inevitable in the long run due to important differences among these nations on how to deal with changing patterns of international trade and investment, long term energy requirements, and political relations with the Third World. However, the nuclear technology question, especially as it has become linked with other outstanding issues, such

This paper was prepared by the Office of Regional and Political Analysis in the Western European and International Issues Divisions. Comments or questions will be welcomed.

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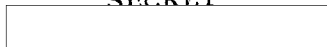


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as human rights, has acted as a catalyst to speed up the pace of change and served as a lens to focus attention on immediate costs and difficulties.

The two papers that follow analyze possible directions the nuclear controversy might take. They assume that issue has not yet been finally settled and that the question of whether either Brazil or West Germany might yet yield to US pressure remains open. To this end the papers devote most of their attention to an assessment of the likely consequences of alternative scenarios. They are intended more to illustrate the kinds of factors that the relevant actors will consider, than to predict the eventual outcome.

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BRAZILIAN REACTIONS TO US ATTEMPTS TO RESTRICT ACCESS
TO SENSITIVE NUCLEAR TECHNOLOGY: FUTURE SCENARIOS

The controversy among Brazil, West Germany, and the US over the advisability of the sale of sensitive nuclear technology by West Germany to Brazil could evolve in several different directions. This article will assess probable Brazilian reactions to three possible scenarios: Increased US pressure on Brazil to accede, a decision by West Germany to yield, and a decision by the two countries to proceed despite US desires. An alternate scenario, which involves postponing to some future date the decision as to whether sensitive technology will actually be passed, will be mentioned but not discussed in detail since the Brazilians are unlikely to accept any degree of prolonged ambiguity in the resolution of this issue.

Increased US Pressure on Brazil to Unilaterally Accede

Brazil almost certainly will not yield to US incentives, diplomatic pressure, or minor economic sanctions and give up both the uranium enrichment and fuel reprocessing technology contracted for from West Germany. The possibility that they would negotiate on the basis of giving up one part of the fuel cycle (e.g., reprocessing but not enrichment) is only slightly greater.

In effect, virtually all important Brazilian leaders emphatically believe Brazil needs the technology for essential economic, political, and prestige reasons. Above all, they seem convinced that they cannot permit the perception that Brazil is yielding to US pressure. These opinions are held by President Geisel, his closest advisors, and [redacted] by all top military commanders. In Brazil's authoritarian and very hierarchical, military-dominated political system it will be these individuals who make the central decisions on this nuclear issue.

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Some nervousness about jeopardizing Brazil's relations with the US by remaining intransigent on

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renegotiating the nuclear accord has been expressed by individuals such as [redacted]

[redacted] how-
ever, has little political influence within the present government. And, if he attempted to express his opinion forcefully even within closed circles, he would probably be dismissed from his post.

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Concern about the cost of the 1975 accord with West Germany, the feasibility of the sensitive technology, and the danger of straining relations with the US has emanated from some officers at the Superior War College, a few nuclear technicians and atomic physicists at NUCLEBRAS (the government nuclear energy agency) and organizations such as the Brazilian Society of Physics, and from some sectors of the business community. But these individuals and groups will almost certainly have no substantial influence on the current deliberations of Geisel and his closest advisors and military supporters.

While obviously concerned about US intentions, the inner circles of the Brazilian government apparently do not believe that the US will exert major economic pressure on them to force them to yield on this issue. Publicly they also take the position that the US government is powerless to prevent the private and public foreign sectors from continuing to support the economic growth of Brazil. They assert that commercial banks, international financial institutions, and other investors will continue to make their judgments purely on economic grounds, and US government actions cannot undermine Brazil's good credit rating.

In fact, however, in at least the short term the Brazilian economy may be quite susceptible to major US economic sanctions, such as the introduction of non-economic criteria as a basis for deciding US votes on loans and other financial assistance to Brazil by international financial institutions. It is unlikely that these kinds of sanctions, even if they began

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seriously to undermine investor confidence in Brazil, would cause an immediate capitulation by the Brazilian government. But there is a chance that the imposition of major sanctions would cause a basic split in the military high command. Such a division between those willing to modify the Brazil-FRG agreement to save the economy and a more nationalistic group unwilling to back down at any cost might eventually result in victory by the former, and a decision to forego the technology. But the ultimate political consequences of such a split would be considerably broader. Political stability in Brazil under the current authoritarian regime depends above all else on the maintenance of a high degree of unity within the military. The loss of this unity could usher in a period of prolonged political and economic instability.

West Germany Unilaterally Yields

If West Germany responds to US pressure and unilaterally cancels the transfer of sensitive technology, the most immediate decision for the Brazilian government will be whether to annul the remainder of the agreement. It is not a foregone conclusion this will happen. But the pressures to do so will be very strong. The intense nationalistic reaction in Brazil to the loss of the technology will call for some kind of retaliatory reaction. Undoubtedly much of the antipathy will be directed against the US as the ultimate author of the West German decision although Brazil is quite limited in its options for striking hard at the US. The cost that can be inflicted on West Germany by cancelling the rest of the agreement, however, is substantial, immediately available, bound to be popular, and not likely to draw retaliation from the Germans. Moreover, the damage to the Brazilians nuclear program caused by cutting the ties with the Germans might be seen as acceptable by the Brazilians since they probably believe other suppliers will be eager to replace the Germans as a source of nuclear reactors. Finally, some Brazilian

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nuclear experts believe that Brazil, if forced to, has the capability to develop a natural uranium based nuclear reactor industry which would not be dependent on foreign technology. Although they may underestimate the effort, expense, and time necessary to accomplish such a program, this belief probably reinforces the notion that Brazil can afford to be unyielding with both West Germany and the US on obtaining access to the full nuclear fuel cycle.

Brazil is unlikely to accept any degree of indecisiveness on West Germany's part as to whether or not the sensitive technology will actually be transferred. The West German's might provide private assurances to the US that they have not made a final decision to pass certain parts of the sensitive technology to Brazil, either to relieve US pressure on them or because they are actually reassessing the advisability of enabling the Brazilians to enrich uranium or reprocess spent fuel. Any intimation of this position to the Brazilians, however, would probably cause a severe reaction. It is likely that the Brazilian government would first issue an ultimatum to the West Germans rejecting any delay, and they would privately (or possibly even publicly) establish benchmarks to judge whether the Germans were keeping their part of the agreement. A failure by West Germany to adhere to this schedule would probably trigger the same reaction as if the Germans had announced cancellation of the transfer of the sensitive technology.

Brazil and West Germany Proceed

If, despite US expressions of opposition, Brazil and West Germany decide to proceed with full implementation of their agreement, Brazil's domestic and international politics will be affected. The public perception that Geisel has successfully defied the US is likely to elevate his popularity to the point that his government will be able to control the 1978 congressional elections and 1979 presidential succession without concern over civilian political reaction or fear of division with the military. He would probably also be able to use this broad political

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support to reduce to easily containable levels the resentment in business and other circles that is building over the economic austerity program he intends to implement over the next year or so.

Internationally, the appearance of successfully opposing the US on an issue of such prominence would probably boost Brazil's prestige among developing countries generally and would carry particular weight within Latin America. It would be perceived as an indicator that Brazil is steadily moving towards the major power status it desires not only economically but also in political terms. A logical consequence of acquiring enhanced prestige would be for Brazil to attempt to pursue new leadership initiatives, acting more boldly as a spokesman for developing countries during negotiations with the industrial countries than it has in the past. The Brazilians might speak out with particular vigor on the need, from their viewpoint, to modify the decision making procedures of international institutions. Their goal would be to curb the power of the US and the other industrialized countries to use international organizations to achieve their political goals on matters, for example, such as human rights and controlling nuclear technology spread among developing countries.

Relations with the US would also be affected. Having succeeded once in withstanding US pressure on a contentious issue, the Brazilians would become more confident that they could do so again in the future should the need arise. At the same time, however, as long as the Brazilians did not feel that the US was taking measures against them in trade or other bilateral sectors to "punish" them for their victory, they would probably signal a willingness to return to business-as-usual. While some nationalistic elements (including some among the hard line military) might attempt to press Geisel to orchestrate a broad anti-American campaign on other issues, Geisel would probably feel Brazil's interests would be better served by guarding against the injection of emotional nationalism into these areas.

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POLITICAL AND ECONOMIC IMPLICATIONS OF BRAZILIAN NUCLEAR
DEAL FOR US-WEST GERMAN RELATIONS

The disagreement between the US and West Germany concerning the sale of a complete nuclear fuel cycle to Brazil is one of the most divisive issues to affect the Alliance partners in the post-war period. Chancellor Schmidt's announcement on March 30 that West Germany intends to proceed with the sale despite US objections indicates his willingness to risk an open confrontation with Washington at a time when the American-West German relationship is buffeted by other troublesome issues.

The West Germans, in addition to their economic stake in the Brazilian deal, view it as a critical political problem having wider dimensions. First, the Schmidt government has concluded that the Carter administration shares the previous US position that the Federal Republic can and must play a major role on the international scene. Although aware of the special nature of the problem of nuclear proliferation, West German officials feel the US demands pertaining to the Brazilian deal are only the latest in a series of requests that burden the Federal Republic with added obligations within NATO and the Western industrial community as a whole. From the West German perspective, the dispute over the Brazilian deal in effect amounts to a test case of what kind of relationship Washington wants with its most powerful and reliable ally. The West Germans pose the question in these fundamental terms because they are generally unwilling to consider the Brazilian deal as a policy issue that stands apart from the other important elements, particularly the security tie, that make up the bilateral relationship.

The West German perception that President Carter wants to change the substance as well as the style of American foreign policy is the second factor influencing

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Bonn's reaction to Washington's reservations concerning the Brazilian deal. Whereas many West Germans initially felt that US objections were merely a sanctimonious facade for competing American commercial interests, most officials in the Schmidt government, including the Chancellor himself, acknowledge that the US position on non-proliferation reflects genuine moral and humanitarian concerns. In fact, the political elite in Bonn assumes that this moral-humanitarian viewpoint will ultimately influence US policy on other issues that touch directly on West German interests, such as the negotiations on strategic nuclear weapons and troop reductions in Central Europe. From this perspective, Washington's reservations about the West German-Brazilian nuclear project appear to be merely one manifestation of an across-the-board change in US foreign policy.

The precise implications of American policy for West German interests in the Brazilian deal and other issues are still a matter of speculation in Bonn. West German officials are clearly perplexed because the apparent US desire that the Federal Republic assume a larger role on the international stage is coupled with a request which, in their opinion, threatens the biggest single commercial venture for West Germany since the war. Chancellor Schmidt, in any case, appears ready to risk some damage to the bilateral relationship in order to preserve the Brazilian nuclear project. Considerable national prestige is at stake for West Germany as well as Brazil. The West Germans argue that to renege on the commitment to deliver a complete nuclear fuel cycle would make it extremely difficult for their country to maintain its reputation as a reliable business partner. Moreover, the contract to sell as many as eight reactors to Brazil represents exactly half of all the foreign orders that the West German nuclear industry has received since its first foreign sale in 1968 and will provide jobs for thousands of West German workers. Cancellation of the contract would keep unprofitable a high technology industry that Bonn considers to have high growth potential and in which the government already has invested \$8 billion.

Apart from this joint nuclear project, the West Germans hope that Brazil will become an important trading partner and help open up the entire Latin American market to German goods. Today Brazil absorbs only 1% of West German exports and 7% of its investments worldwide. However, West German exports

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to Brazil have grown nearly twice as fast this decade as overall German exports. Brazil already accounts for nearly one quarter of West German investment in LDCs--some \$1.3 billion as of June 1976.

Although these arguments imply that any modification of the contract with Brazil would be disastrous for the Federal Republic, the political and economic impact on West Germany will vary widely depending on the final outcome of the current consultations among the three countries. What follows is an analysis of the three most likely outcomes from the West German point of view.

Brazil Backs Down

The first scenario assumes that the US somehow succeeds in persuading Brazil to forego the purchase of the sensitive nuclear facilities or to accept an alternative arrangement. This would be the preferred solution from the West German standpoint if the US remains adamant. The Schmidt government would escape international criticism that it did not honor a contract and at the same time preserve good relations with the US. This solution requires that Bonn not appear to have taken any part in putting pressure on Brazil. Domestic criticism of the Schmidt government under these circumstances would be minimal, or at least, easy to contain. West Germany officials would probably accentuate the positive and argue that the sale of eight reactors still guarantees the Federal Republic will reap the lion's share of the economic gain envisioned under the original contract. Indeed, the commercial loss resulting from the non-sale of sensitive nuclear facilities would be marginal.

Some West Germans, primarily those of leftist persuasion who usually vote for the Social Democratic Party, might praise the Carter Administration for its successful effort to halt the transfer of this sensitive technology and thereby help prevent the spread of nuclear weapons. There would, nevertheless, be a residue of bitterness in many political and business circles which would feel the ex post facto modification of the contract with Brazil automatically casts aspersions on the original West German intentions. This reaction would be equally strong among conservatives in the opposition and the government. Resistance to US requests for financial participation in other international projects such as the creation of an airborne early warning system for NATO would certainly increase.

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Bonn "Caves In"

A quite different scenario would develop if the Schmidt government retreats from its present headline position which would probably only occur as a result of the most intense US pressure and decides to delete unilaterally the sensitive nuclear facilities from the contract with Brazil. This action, in the face of Brazilian insistence that the contract be honored, would provoke a sharp outcry in West Germany. Although the opposition parties--the Christian Democratic Union and the Christian Social Union--have a long history of staunch pro-American sentiments, their immediate reaction would be one of dismay. Opposition leaders would criticize Schmidt sharply for reversing his position and jeopardizing the entire project. The Union parties, of course, would be in an ideal political situation because they would bear no responsibility for making the difficult choice between satisfying the US and fulfilling the commitment to Brazil.

Government officials, meanwhile, would have to work hard to maintain unity within the Social Democratic/Free Democratic coalition. The Free Democrats have close ties with the business community and traditionally defend its interests. The turmoil within this pivotal party would be considerable because the national chairman, Foreign Minister Genscher, committed his personal prestige when he signed the contract with his Brazilian counterpart two years ago. There might, however, be widespread sympathy for Schmidt and Genscher if the public believed that the US had threatened drastic consequences for the security relationship to get the West Germans to cooperate. In these circumstances, opposition leaders and disaffected individuals within the government would have to think twice about trying to capitalize on Chancellor Schmidt's dilemma.

Reaction abroad to the Schmidt government's retreat would vary widely. Many countries such as Canada, the Netherlands, and the USSR, which favor strong safeguards against nuclear proliferation, would endorse the West German action. The response would be similar in France, though the Giscard government would have to be more cautious in its statements because many West Germans have a sharp

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eye for any hints that French industrialists would be encouraged to steal the rest of the Brazilian contract for the reactors.

Reaction among underdeveloped nations which need assistance in building nuclear energy programs would be undoubtedly negative. Many would be sharply critical, asserting that Bonn and Washington have formed a condominium to keep the "have-not" countries poor.

The political fallout would again probably be manageable if Brazil quickly agrees to buy the eight reactors and forego the sensitive technology. The damage to the West German economy would also be minimal, denying Schmidt's critics a large part of their case against the government. Many West Germans, nevertheless, would be extremely bitter toward the US for forcing Bonn to knuckle under. In this regard, the psychological impact could be enormous for the younger of the German leaders who had to a certain extent outgrown the feelings of extreme dependence on the US characteristic of their elders. The reaction would take various forms, but many would harbor deep feelings of resentment toward the US for having humiliated them and the Brazilians. This might strengthen Bonn's reluctance to cooperate with Washington on other matters where there are differences.

The political and economic repercussions in West Germany would magnify if Brazil followed through with its threat to cancel the entire contract. The loss of the projected sale of eight reactors would seriously jeopardize West Germany's nuclear construction industry, which already faces a shrinking domestic market. Kraftwerk Union must sell 6-7 reactors each year, at home or abroad, to be profitable. Indeed, the Federal Republic must make a breakthrough in this and other high technology or capital-intensive fields if German industry with its high-wage labor force is to remain competitive in foreign markets. Cancellation of the Brazilian deal could mean the loss of 20,000 jobs in the nuclear industry, and perhaps many more in related

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industries. This would increase the unemployment rate which Bonn already considers high at 4.4 percent.

The possible collapse of the Schmidt government under these circumstances cannot be completely ruled out. Foreign Minister Genscher would have a difficult time in rationalizing the government's retreat to conservative Free Democrats who might be tempted to use the Brazilian issue as a pretext for striking a deal with the Union parties. The scenarios are nearly limitless, but it would, in any case, only take six defections to give the Christian Democrats an absolute majority in the Bundestag.

Many Christian Democrats, however, would be reluctant to assume power in these circumstances. Defenders of the Schmidt government would undoubtedly accuse the conservatives of riding a wave of public reaction against Washington's "strong arm" tactics--a very distasteful situation for the Christian Democrats who place the highest value on good relations with the US. The Brazilian issue cuts across all party lines to such an extent that an alternative to the present coalition might be impossible to form. The West Germans might resort to early elections as a way out of the impasse.

Schmidt Defies the US

The third scenario assumes that Chancellor Schmidt, with the full support of Foreign Minister Genscher, follows through with the declaration to go ahead with the nuclear project with Brazil. Schmidt's decision would be a calculated gamble based on two assumptions.

- First, the current widespread public support for the government will hold fast. The opposition parties in fact could hardly attack the Chancellor after having urged him to resist US pressure to modify the contract.

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- Second, the expectation that the Carter Administration on balance would decide not to retaliate against Bonn for defying US wishes.

Many West Germans would be nervous about playing such a bold game in view of the leverage that the US has long been presumed to have over the Federal Republic. This traditional assessment, however, has come under revision in the past two or three years, at least in the minds of some high-level West German officials. The broad debate concerning the "New Germany" and its special partnership with the US has had the effect of strengthening the confidence of those West Germans who believe that Washington needs Bonn as much as Bonn needs Washington. The Schmidt government would find it difficult to believe the Carter administration would retaliate against its strongest ally when its support is crucial for other US policies.

The economic benefit from this bold course of action would be considerable. Kraftwerk Union would be guaranteed the orders for the eight reactors which would ensure the industry's viability at least for a few years. West Germany would gain access to any uranium found in Brazil for use in the Federal Republic's extensive nuclear energy program.

The political consequences from the Schmidt government's decision to defy the US over nuclear proliferation are more difficult to predict. Other Europeans, including the Soviets, would be disturbed by the Federal Republic's ability to resist the US on such a sensitive issue. Under these circumstances, the debate about the "New Germany" would inevitably lead to speculation about Bonn's aspirations. Indeed, the Schmidt government's unwillingness to stimulate the German economy as much as Washington would like, coupled with controversy over the Brazilian issue, has already dramatically transformed the atmosphere of US-West German relations. Some West German officials might be encouraged to play hard ball with the US on other contentious issues.

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The overall impact of the Schmidt government's action, however, would be uneven. Most West Germans, particularly those who are strongly pro-American would be nervous about the implications of their "success" against the Carter administration. The Federal Republic is still weak in geo-strategic terms and will be dependent on US military support for the foreseeable future. Political realism would limit the degree to which some West Germans might want to test Washington's forbearance. It is unlikely, therefore, that Bonn would choose to be deliberately uncooperative with Washington on other issues.

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