

The Mexico debt crisis and the International Monetary Fund

by David Goldman, Economics Editor

Western central banks, at the behest of the U.S. administration and Federal Reserve Chairman Paul Volcker, have arranged an unprecedented \$1.5 billion loan to Mexico, which ran out of cash and imposed full exchange controls Aug. 13; the central-bank package is additional to \$2 billion in cash (oil prepayments and agricultural credits) from the U.S. government.

Whether this package, plus a \$4 billion, three-year credit agreed "in principle" with the International Monetary Fund, will constitute a bailout for the bankrupt debtor, whose \$80 billion in private-bank obligations are sufficient to bring down the Western banking system, was fought out at a meeting Aug. 19 and 20 held at the New York Federal Reserve Bank, attended by Mexico's major commercial-banking creditors. In essence, Mexico received the \$3.5 billion to relieve immediate cash needs on its estimated \$500 million per week interest debt service, but only a 90-day rollover of the principal.

The 'debt bomb' dimension

No details are available at deadline concerning the terms which Mexico will pay for the rescheduling, but doubt has emerged in the minds of the creditors about whether they may turn Mexico into the bloody example that the International Monetary Fund staff originally wanted, i.e., eliminate not merely all government subsidies of basic consumption items but break the institution of the presidency and the political power of the Mexican labor movement, which implies a

violent constitutional change. The threat of the "Ibero-American Debt Bomb," a proposal associated with this publication's founder, Lyndon H. LaRouche, Jr., and now a matter of highest-level discussion among Argentina, Brazil, and Mexico, has become a matter of sober evaluation in the public press.

Le Monde of Paris editorialized on its front page Aug. 18, "Individually, Mexico, Brazil, and Argentina appear weak; but they could turn their individual weakness into collective strength by combining against their creditors." And the London *Guardian* wrote Aug. 16, "Some economists argue that the present high demand for credit is caused by this desperate need to borrow to pay off interest, which in turn keeps interest rates high—a particularly vicious circle. One logical way out of this is for developing countries not to reschedule—which leaves them still paying the interest—but to deliberately refuse to pay anything. Interest rates would come tumbling down, but so would world economic activity and the weaker Western banks."

The *Guardian* comment concluded, "This shock would hurt us more than them, and the day may come when a big debtor is tempted to do it." That evaluation is accurate, even in the case of Mexico, 70 percent of whose industrial sector depends on re-assembly of imports from the United States.

Federal Reserve officials insist that a moratorium declaration for Mexico, even conjointly with other Latin American nations, would represent a messy form of suicide, since the United States would allegedly respond with a full trade boy-

cott. The threat is less impressive for Argentina and Brazil, whose economies are relatively more self-sufficient, than for Mexico's fundamentally flawed import-substitution economy. However, under the terms the International Monetary Fund has demanded, Mexico would have nothing to lose in any event, and might gain from regional integration with the rest of Latin America.

In short, the Fed and the IMF are bluffing, and the British and French press have gone to the extreme length of pointing this out to them in public print, in the midst of the most brutal negotiations over the future of the monetary system since the quadrupling of oil prices in December 1973 exposed the weakness of the world credit system.

Annual IMF report

This public exchange tells more about the behind-the-scenes debate in the central banking circuit and at the two international institutions, the International Monetary Fund and Bank for International Settlements, which propose to "manage" the crisis, and steer it towards a world financial dictatorship. No less than the latter conclusion must be drawn from the black-and-white statement of the IMF's just-issued Annual Report, which demands the maintenance of tight monetary policies in the Western nations, and the elimination of such "structural rigidities" as wage levels protected by government subsidies, among those the IMF specifies by name. Mexico's case, in which the IMF is demanding reductions of living standards (through elimination of subsidies and union-busting) of a sort that no *constitutional government* in Mexico could tolerate, strikes equally at West Germany, where the Schmidt government is maneuvering to use government guarantees to prevent the liquidation of a 120,000-person employer, Germany's sixth-largest employer, the AEG-Telefunken group (see article, page 11). Ultimately, the "international institutions" aim at the program of the 1922 Genoa Monetary Conference: no government might obtain credit or spend money without IMF approval, and no commercial bank might lend money without BIS approval, the ultimate "one-world federalist" dictatorship.

The IMF report "urges a comprehensive policy approach in the fight against inflation and unemployment. It cites the importance of various rigidities and structural imbalances that have become imbedded in the economic system, especially with respect to wage bargaining, price setting, and certain aspects of government spending and taxation. . . . The approach required would need to include measures designed to reduce or eliminate existing rigidities and structural imbalances in the fiscal field, in the goods and labor markets, and in other problem areas, such as regulatory burdens and excessive subsidization or protection of ailing industries," stated an IMF press release of Aug. 22. The report also demands "both maintenance of restraint in financial policies and public conviction that such policies will not be reversed."

Ultimately, the report concludes, the meatgrinder into which national economies pass will churn out "stable ex-

change rates," a program otherwise circulating under the label "a New Bretton Woods System," named after the 1944 agreement that reset fixed exchange rates and lasted until America floated the dollar in 1972. "While recognizing that it is impossible to achieve stable exchange rates as long as inflation is not under control, the report points out that the stability of exchange rates could be enhanced by achieving greater control of budgetary deficits, while continuing to pursue prudent monetary policies; by reducing structural rigidities in wage bargaining and price-setting mechanisms; and by adopting some flexible forms of incomes policy." In other words, under the pretext of the Versailles agreement to work for greater stability of exchange markets, the IMF proposes to dictate policies to national governments which no government might accept, in effect becoming a form of world government itself.

For Mexico in particular, a secret June 25 IMF Staff Review of the Mexican economy stated, "The public-sector deficit in 1982 would be in the neighborhood of 11 percent of GDP, and thus would continue to require financing on a scale that has to be viewed as exceptional and unsustainable. Clearly, further large reductions in the public-sector deficit will have to be made in the near future to lessen the risks of high inflation and severe balance of payments pressures. The adjustment of public-sector prices [e.g., subsidized basic items' prices—D.G.] to realistic levels and the elimination of subsidy payments out of the budget should be expected to play an important role in the correction of the fiscal imbalance."

Who will 'exploit' the crisis?

No one is better aware than the IMF that the \$600 billion-plus overhang of developing-nation debt is unpayable, and liable to ruin debtor and advanced-sector creditor alike, unless the two agree to a form of rescheduling that promotes international trade and aids in restoring the depressed industrial economies, of the form this publication advocates. The IMF does not propose to *prevent* such a crisis, but to *use it* to increase its own powers and those of its semi-private sister institution, the Bank for International Settlements (BIS).

From this vantage point, the central-bank bailout of Mexico has a double significance. Mexico failed to activate the debt weapon, and, whatever the final IMF terms, will pay brutally for dealing with the international institution; but the *threat* of the debt weapon has been sufficient to persuade the Reagan administration and the central banks themselves to throw their monetarist scruples to the wind, and hand over some \$3.5 billion Mexico could not obtain otherwise. In short, they have decided to paper over a general banking collapse visible for the September period, as Lyndon LaRouche suggested they might (see *EIR*, Aug. 24), postponing matters to next January or February at the latest. The fact of the bailout itself puts the BIS on the map in a way it could not previously claim, as the agency to which the U.S. government itself must go to deal with a crisis on its border that

threatened the American banking system (some \$48 billion of Mexico's \$80 billion public and private debt is to American banks). But the central banks' largesse to Mexico, even though it will benefit only the country's creditors and not the country itself, nonetheless hauls into public view the exposed weak flank of the international institutions and their associate banks: the debt bomb would "hurt us more than it would hurt them," as the *Guardian* and *Le Monde* admitted.

"Mexico did not roll over and die," commented a senior official at the General Agreement on Trade and Tariffs headquarters in Geneva. "They still have resources they may draw on." But even if Mexico staves off the most exorbitant of the IMF's demands, the state of the world economy alone implies a profound crisis for that nation. Whatever concessions it must make to the IMF will deepen that crisis.

The exposure of the central banks' weakness, however, will not be lost on Brazil, which for the first time is having trouble raising the immense volume of funds it requires to handle a \$80 billion debt burden, nor on Argentina, already \$2.5 billion behind in payments on its \$40 billion debt. Although Mexico was unable or too internally divided to persuade the other two countries to join in a common front against the IMF, the fight has not been won by either side. It will erupt when the central banks' money runs out, that is, before year-end. Meanwhile Brazil and Argentina have a greater incentive to push for favorable rescheduling terms. The debt bomb is still ticking.

From a discussion with a leading GATT spokesman on Aug. 18:

I agree with you completely that the financial system is about to go bust. I am not aware of any contingency plans negotiated between the central banks, except the old BIS Concordat. All bankers I talk to say that the central-bank arrangements are so vague that any sudden crisis would overtake them totally. I do not think that adequate international preparations are in place.

Central banks can be lenders of last resort even for extreme illiquidity. What about insolvency? Large writeoffs for banks mean a negative net worth—bankruptcy. Illiquidity merges into insolvency. If huge sums were to be involved, for this, governments, treasuries, would have to be involved and step in. Then that means virtual nationalization of banks!

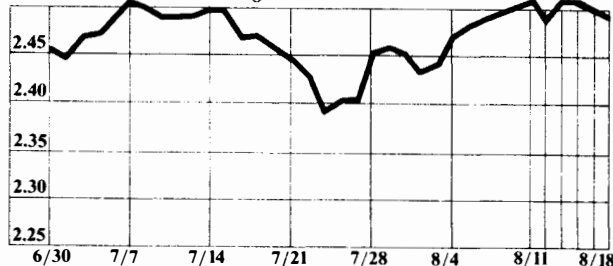
Next we have a timing problem. Sept. 10 is the deadline for renegotiating the 1982 Polish commercial debt. Then the Mexican problem is building up. . . . I expect November and December to be terrible.

Yes, I have heard the same as you concerning Shultz's views on this. . . . But where would the power be behind a McNamara-like world central bank? It could only work with the backing of the main financial powers, the G-10 etc. It cannot work, and if it did it still would not fit.

Currency Rates

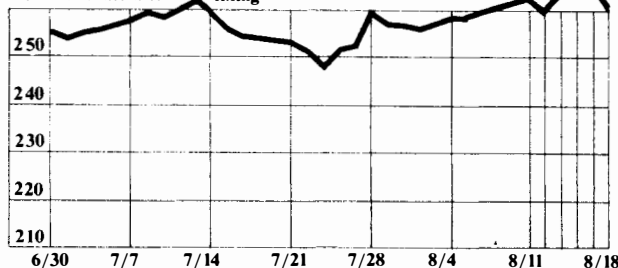
The dollar in deutschemarks

New York late afternoon fixing



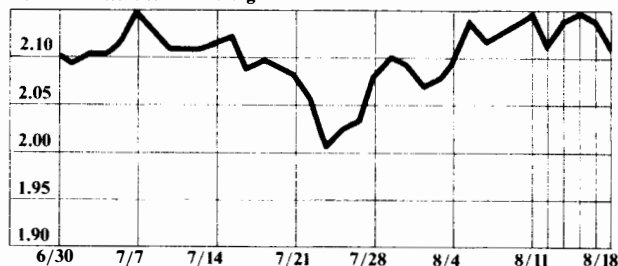
The dollar in yen

New York late afternoon fixing



The dollar in Swiss francs

New York late afternoon fixing



The British pound in dollars

New York late afternoon fixing

