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Brazilian debt crisis rattles credit markets

by Timothy Rush and Dennis Small

Connoisseurs of three-card monte and other street shills got the treat of their lives this month from watching the way the International Monetary Fund and the elite of the international financial community handled Brazil's explosive monetary crisis with pyramids of worthless paper and sleight of hand.

The state-controlled Banco do Brasil, Brazil's largest commercial bank, has gone bankrupt, not once, but twice. On Tuesday, Dec. 7, the New York branch first sent up S.O.S. signals that it could not meet $175 million in immediate foreign currency obligations. The New York Federal Reserve Bank, faced with the prospect that such a default would instantly bring down the entire $200 billion-per-day CHIPS international banking clearinghouse system, preferred to step in with an emergency injection of funds to the Banco do Brasil. But the very next day the troubled bank was again bankrupt. This time, a group of five leading New York commercial banks stepped in with the needed emergency cash.

The Banco do Brasil is normally backstopped by the Brazilian government itself. But the Brazilian government is *also* bankrupt, struggling on a day-by-day basis to pull in enough cash to keep its head above water and meet its payments on its huge $89 billion foreign debt.

Only a week before the Banco do Brasil rescue operation, the U.S. Treasury used the occasion of President Reagan's trip to Ibero-America to announce a special, emergency $1.2 billion "bridge loan" designed to "solve" Brazil's crisis that week. What the Treasury didn't mention was the fact that the $1.2 billion had actually been disbursed to Brazil *six weeks earlier,* and that it was long past spent. Two weeks before that, another $600 million was coughed up by six big New York banks to avoid a Brazilian default at that point.

Even as the Fed and the commercial banks were bailing out the Banco do Brasil, U.S. Treasury Secretary Donald Regan and Secretary of State George Shultz were criss-crossing Europe to try to pull together yet another $1 billion-plus "bridge loan" for Brazil—this one to come from the central banks of West Germany, France, and Great Britain.

All these actions are being billed as "bridge loans" until a Brazilian deal with the IMF comes through. At that point, the IMF money is supposed to repay the interim lenders.

There could be no greater demonstration of the financial genius of the managers of the IMF system. The IMF deal, expected to be initialed Dec. 17 and ratified in early February, would release only $2.0 billion in its first year. The "bridge loans" exceed by at least 50 percent the amount of money waiting at the other end of the "bridge." Furthermore, the Executive Director of the IMF, Jacques de Larosière, has announced that his institution will *not* shell out the promised money to Brazil—unless Brazil's principal commercial bank creditors agree to substantially increase *their* lending to Brazil. Not surprisingly, the banks aren't tripping over each other to throw more money at Brazil, given that the country has twice demonstrated that it was in effective bankruptcy.

Failure at Kronberg

What makes this farce tragic is the fact that the story of Brazil is the story of a half dozen other major Third World creditor nations—Mexico, Argentina, Yugoslavia, and Chile included. There is no conceivable way these nations can continue to meet their inflated debt-service payments while world trade and economic activity continue to spiral down-

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Carlos Namba

An IMF team leaving Brazil's Presidential Palace in November.

ward. But rather than address that underlying problem, the international financial elite has chosen to throw huge sums of money at problems, to firefight as each crisis explodes. The money is of course never seen by the "recipient" countries, but is simply recycled back into the bankrupt world monetary system. Such a game cannot long continue.

The finance ministers of the big five Western nations met Dec. 8-9 at the Schloss Kronberg near Frankfurt, West Germany, to "solve the crisis." The meeting was a failure, as even its participants are now admitting, and served principally to hammer out the details of the latest and biggest "bridge loan" to Brazil.

The only broader approaches even under consideration are:

1) to increase the size of the industrial nations' joint checking account, the General Agreement to Borrow, from the present size of $8 billion to between $15 and $20 billion. Most of those additional funds, however, would be drawn by non-Third World countries like Spain, Sweden, Italy, and Denmark; and

2) to raise the present $60 billion quotas members contribute to the IMF by 50 percent. But of the $30 billion "new" money, only $17 billion would be in hard currencies and therefore lendable.

Even combined, these two "solutions" don't come close to being able to cover the magnitude of financing that Third World debtors require to keep current. The prognosis is for a growing wave of defaults from most debtor nations, and for the world financial system to tremble, and possibly come down in pieces as a result.

When Brazil began formal negotiations with the IMF on Nov. 28, Planning Minister Delfim Netto gave assurances that the Fund would simply give its approval to his existing austerity plan for 1983, with no abrogation of Brazil's national sovereignty. Two weeks later, Brazil's business daily *Gazeta Mercantil* reported that Brazilians were surprised to find it had become "crystal clear the Fund is participating in changing economic policy, making suggestions and approving measures."

Brazil signs with IMF

Brazil hurriedly signed a letter of intent with the Fund Dec. 15. The contents are secret. Conditions agreed upon reportedly include a 16 percent cut in total state investment from this year's budget, in which the nuclear and hydroelectric sectors may be worst affected, but not the one-shot devaluation the IMF had been demanding.

"There is no motive for panic, since we are only discussing our balance of payments," pleaded Sen. José Sarney, president of the ruling Democratic Social Party. But the IMF accord has compounded the despair of Brazilian businessmen already hit in November by record bankruptcies. The London *Financial Times* headline Dec. 17 was "Brazil Industry to Bear Brunt of IMF Accord."

Further de facto conditionalities include:

- *Wage cuts:* The IMF is demanding changes in Brazil's wage-indexing system to reduce real wages by a third. This is so sensitive that no Brazilian official will admit the coming changes in the wage system were forced by the IMF. The result will be social upheaval next year.
- *Oil imports:* After talking to the IMF, the government promised it would make as many added cuts in oil imports next year as necessary to achieve their promised overall $6 billion trade surplus—a figure most observers admit is impossible to achieve in the current climate of world-trade collapse.

The government did not consult with the opposition forces, which won 61 percent of the vote in the Nov. 15 elections, on going to the IMF. In a concise statement, the moderate major party of the opposition (Brazilian Democratic Movement Party—PMDB) warned that "extremely damaging agreements" with the IMF would bring "unbearable social costs falling on a population which already lacks even the essentials for survival. Among its irreparable blows will be increased unemployment, growing inflation, more sacrifices for workers, and ruinous taxes on small and medium-sized Brazilian firms."

The PMDB party, which got more votes than the regime's own party, concluded: "The current problems of Brazil's foreign debt will not be solved under the joint tutelage of the IMF and the U.S. Treasury Department. Recession, unemployment, and greater denationalization of the Brazilian economy, despite its extremely high social cost, will not provide the foreign exchange needed to put our payments in balance.