

# EIR Operation Juárez

## Ibero-America's debt: It's 95% illegitimate

At the end of 1977, the foreign debt of the 20 nations of Ibero-America stood at a worrisome \$125 billion. This represented a three-fold increase over the 1973 level of \$40.0 billion. In the eight years from 1978 to the present, the foreign debt almost tripled again, and now stands at \$370.0 billion, a nine-fold increase over the 1973 level.

The jump starting in 1973 was a direct consequence of the oil shock, which sent a flood of petrodollars rushing into the coffers of the major international banks, which in turn were driven to rapidly place this new liquidity through loans, largely to the unsuspecting nations of Ibero-America. In fact, the mass of debt has grown so rapidly that it has outpaced GNP growth rates during the recent period by 3½ times. The only thing that has kept pace with the debt is the expansion of the illicit narcotics traffic—which is increasingly being suggested by the International Monetary Fund (IMF) and Ibero-America's other creditors as the best way to repay the debt.

Figure 2-1 demonstrates the result of the application of IMF policies: GNP stagnated, the drug trade grew, and the debt went through the roof. Except under the most exceptional of short-term circumstances, austerity such as that demanded by the IMF, as a policy of governments, is incompetent in principle. In the case of Ibero-America, its application has failed to reduce, or even stabilize, the total foreign indebtedness. In fact, the more severe the austerity, the more the need for foreign capital has grown.

However, this result was also intentional. IMF policies, and those of creditor institutions, are *not* principally debt-collection policies. They are policies of using the debt as a lever to accomplish economic and political goals. The world's leading "bankers," in this respect, are not "businessmen." They are ideological *oligarchists*. Their economic goal is the de-industrialization and depopulation of the global economy, starting with that of the Third World nations. Their political goal is the destruction of the sovereignty of nations, an end to the nation-state. And, they are willing to make all manner of special arrangements regarding the debtors' pyramiding obligations, in return for debtor "concessions" that will help them accomplish their goals.

Thus, debt and austerity are means of gaining power over the debtor, not means of ensuring profits per se. Not surprisingly, the bulk of the debt accumulated by Ibero-American nations since 1973, especially since 1978, is found to be illegitimate from any standpoint of sound banking practice. Ibero-America is a continent whose economies have been looted by international financial institutions, by means which have included:

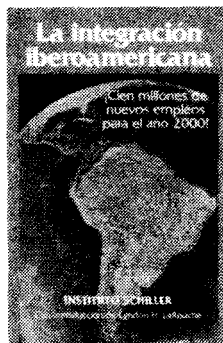
### Part 5

#### Ibero-American integration

By the year 2000 there will be 100 million jobless in Ibero-America, unless the countries of the continent repudiate the policy of "adjustments" and "conditions" of the International Monetary Fund and World Bank.

In this book the reader will encounter a scientific program to meet the crisis. Prepared by an international group of specialists of the Schiller Institute at the request of the institute's Ibero-American Trade Union Commission, it is a study of the urgent means that will free Ibero-America of its economic dependency. The formation of a "debtors club," the physical integration of the continent by great infrastructure projects, and the creation of a Common Market are the first steps toward shaping an virtually self-sufficient economic superpower.

Released in September 1986 in Spanish by the New Benjamin Franklin House of New York, the book is being made available exclusively in English through EIR's serialization.



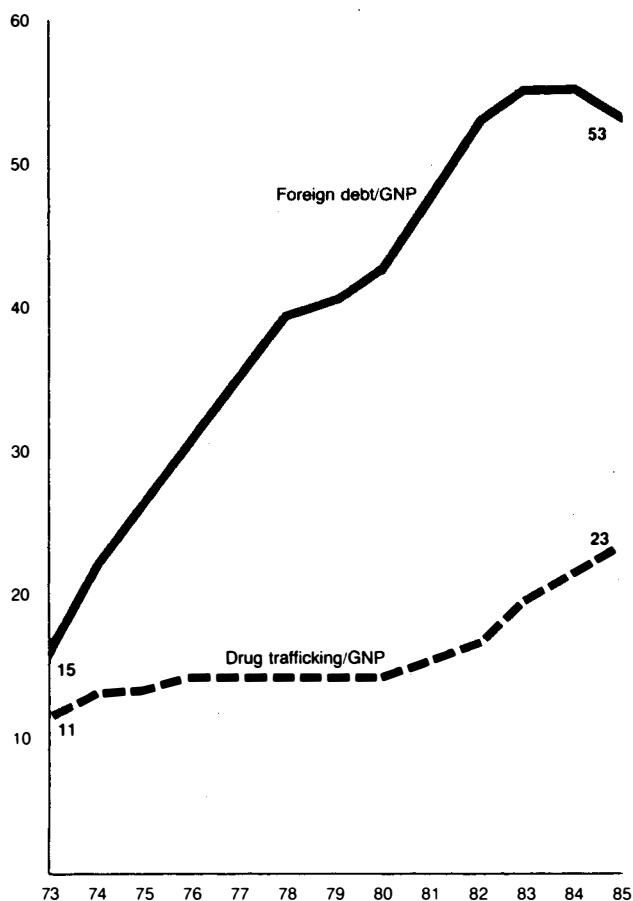
- High interest rates, dating from the onset of the Volcker regime at the U.S. Federal Reserve; in the course of refinancing, debtor nations have been paying steadily higher interest on interest, as well as principal.

- Worsening and unjust terms of trade, increasing the prices which Ibero-American debtors have paid for imports, while reducing the prices they have received for exports.

- Organized flight-capital operations, as a rule carried out by the same foreign banking institutions holding Ibero-American debt instruments.

Therefore, despite a 50% cut in the physical volume of imports and the export of everything not nailed down to earn means of payment, Ibero-America's debt has continued to rise, while tens of billions in development projects have been canceled, industrial sectors decapitalized, millions thrown out of work, roads, services, housing, and sanitation col-

FIGURE 2-1  
**Growth of the foreign debt and drug trafficking in Ibero-America 1973-85**  
 (percentages of GNP)



Sources: Economic Commission for Latin America (U.N.) and authors' estimates.

TABLE 2-1

**Foreign debt and trade balance of Ibero-America 1978-85**

(billions of dollars)

	1978-1981	1982-1985	1978-1985
Increase in debt	157.2	87.3	244.5
Balance of goods	-5.5	114.0	108.5
Trade balance	-26.5	105.2	78.7

Source: Economic Commission for Latin America (U.N.).

lapsed, and large sectors of the population are being driven to the edge of starvation.

Simply, the debt of Ibero-America today, after years of human suffering, is unpayable. Anyone who would insist on repayment, under present conditions, is insisting on genocide by economic means.

**Debt as a looting mechanism**

It has been the prevailing explanation of bankers and their press that Ibero-American indebtedness is a consequence of "profligate spending" by governments which sought to finance "overly ambitious development projects." Were that the case, the figures would show that the nations of the continent imported considerably more than they exported during the period of steepest debt accumulation, 1978-85. That is, they would show a trade deficit to supply supposedly over-ambitious development efforts. The figures show the opposite. Between 1978 and 1985, Ibero-America ran a sizable trade surplus. From 1978 to 1981, there was a slight deficit in goods, \$5.5 billion, and of goods and trade-related services of \$26.5 billion. But this is to be compared to an increase in the debt of \$157.2 billion over the same period (Table 2-1).

Since 1981, even this small deficit has turned into a surplus of \$114.0 billion in goods, \$105.2 billion if trade services are deducted. During this period, \$87.0 billion was added to the debt.

Therefore, excessive imports had nothing to do with the debt accumulation.

An honest examination of the curve of Ibero-American indebtedness prompts the question: What did all the money borrowed go for? The answer, as indicated, is *nothing*. Since 1978, the year that dollar interest rates began their climb, payments of interest alone have totaled \$237.2 billion, while the total increase in indebtedness has been \$244.5 billion. All but \$7.3 billion of the debt increase, in effect, has gone to pay interest.

Until 1982, money was borrowed to fully capitalize interest, plus additional money was used to cover capital flight and small trade deficits. Since 1982, a large trade surplus has paid off some of the interest, while an additional \$90.0 billion in borrowings covered the remaining interest plus additional capital flight. Thus, \$244.5 billion was borrowed to pay off interest and replace flight capital—none of it went to finance

TABLE 2-2

## Growth and applications of the Ibero-American foreign debt

(billions of dollars)

	1978	1979	1980	1981	1982	1983	1984	1985	Total
Total debt	156.5	183.9	226.4	282.7	322.8	343.7	361.4	370.0	
Increase in debt	30.9	27.5	42.5	56.3	40.1	20.9	17.7	8.6	244.4
Interest paid	10.4	15.7	23.0	33.8	39.9	36.4	41.6	36.4	237.2
Trade balance*	-8.2	-4.5	-5.8	-8.0	3.7	29.9	40.5	32.0	78.7
Capital flight	4.9	1.5	14.0	20.4	24.1	14.0	5.8	4.8	89.5

\*Balance of goods and services excepting interest.

Sources: Economic Commission for Latin America (U.N.) and authors' estimates.

development. On top of this, an additional \$79.0 billion was paid out in the form of a trade surplus.

A careful analysis of the balance of payments shows that during this time period, nearly \$100 billion of the new debt of \$244.5 billion incurred cannot be accounted for by flows captured in the balance-of-payments figures. The increase in debt was duly registered, but no corresponding inflow of capital in any form, reported new loans or otherwise, was recorded. Small portions of this may be explained by such things as disguised or unreported arms-purchases by governments. But the preponderance of this sum was flight capital in its many forms.

Bankers financed nearly \$100 billion without apparent concern for what their money was going for: It never showed up as a capital inflow to Ibero-America, much less as a capital outflow.

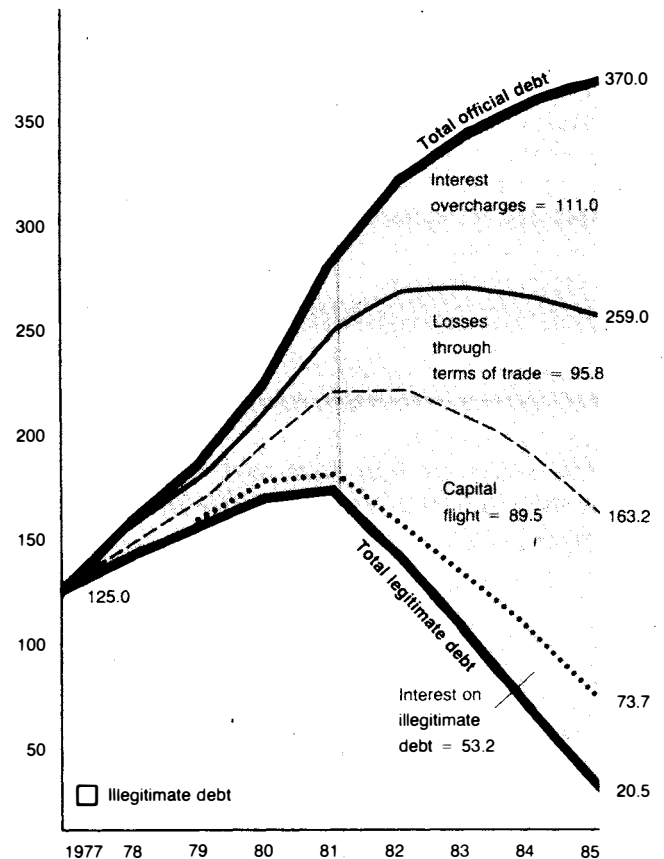
Table 2-2 shows what the total inflow of capital paid for: slight trade deficits in 1978, 1980, and 1981; the annual services deficit; interest on the debt; and capital flight. The international banks' loans to Ibero-America were thus purely speculative, unsecured by tangible wealth, merely capitalizing interest, covering current consumption deficits on the services account, unsecured borrowing against "leakage" of funds through capital flight, or were totally fictitious loans that either never left the bank vaults, or were illegally transferred to accounts outside the debtor countries. In 1982 and 1983, the latter flight-capital category far exceeded registered capital movements, totaling almost \$40.0 billion.

As Table 2-2 shows, virtually no "banking" in the traditional sense has taken place with respect to Ibero-America for at least eight years. The majority of total "loans" have been essentially only a bookkeeping exercise, in which banks have credited themselves with fictitious interest payments by debiting the books of the relevant governments. Additional unsecured loans were made to central banks, but led to no transfer of goods. Most such money returned to the lending institutions as flight capital.

Figure 2-2

## Foreign debt of Ibero-America, legitimate and illegitimate 1978-85

(billions of dollars)



Sources: Economic Commission for Latin America (U.N.) and authors' estimates.

Beginning in 1982, a year of large-scale capital flight out of Mexico and several other countries, the austerity programs that have brought the continent to its knees took hold, and the region began running sharp trade surpluses. From 1982 onward, there has been a flow of real resources, not bookkeeping paper, out of Ibero-America into advanced-sector nations, in the form of exports not balanced by imports. This real transfer of wealth (trade balance line in Table 2-2), totaled \$105.2 billion from 1982-85.

Yet even these figures do not accurately reflect the full magnitude of the looting. An additional form of transfer of wealth has been caused by deteriorating terms of trade. Adjusting both exports and imports to correct for this deterioration gives a total of \$95.8 billion in lost export revenues for Ibero-America since 1978. This represents direct wealth acquired by the advanced economies as a result of unfair trade prices.

TABLE 2-3

### Looting of Ibero-America through interest overcharges 1978-85

(billions of dollars)

	1978	1979	1980	1981	1982	1983	1984	1985
1. Total debt	156.5	183.9	226.4	282.7	322.8	343.7	361.4	370.0
2. Interest paid	10.4	15.7	23.0	33.8	39.9	36.4	41.6	36.4
3. Implicit interest rate (2 ÷ 1)	7.4%	9.2%	11.2%	13.3%	13.2%	10.9%	11.8%	10.0%
4. Interest calculated at 6.8%	9.6	11.5	13.6	16.3	18.4	19.0	19.2	18.5
5. Interest overcharges (2 - 4)	0.9	4.2	9.4	17.5	21.5	17.4	22.4	17.9
6. Cumulative overcharges	0.8	5.1	14.4	31.9	53.4	70.8	93.2	111.0
7. Debt without overcharges (1977) (6 - 1)	155.6	178.9	212.0	250.8	269.4	273.0	268.2	258.9

Sources: Economic Commission for Latin America (U.N.) and authors' estimates.

### The debt is illegitimate

We have shown the way the foreign debt has covered up a process of looting of Ibero-America. But more can be proven: The debt itself is almost entirely illegitimate.

The balance-of-payments and terms-of-trade figures were used to recalculate the post-1977 debt of Ibero-America from the standpoint of constant 1978 interest rates, constant terms of trade, and elimination of flight capital—minimal conditions had a just world economic order prevailed. If we recalculate the debt from 1977 forward under such assumptions of equitable treatment, the conclusion is that there would be little or no Ibero-American foreign debt at all today.

The total Ibero-American debt would have risen to a maximum of \$175.0 billion in 1981 from \$125.5 billion in 1977, before starting to fall, to \$20.5 billion by 1985, and effectively zero by mid-1986. Moreover, this calculation is conservative: It assumes much less capital flight than may have occurred (Figure 2-2).

For purposes of calculation, the illegitimate debt is broken down into four components:

- 1) the direct additional burden in interest and capitalized principal from interest rates above the levels of 1977;
- 2) the effect of deteriorating terms of trade;
- 3) the estimation of flight capital; and
- 4) the compounded interest paid on the debt resulting from the latter two factors.

**1) The interest-rate factor.** All developing-sector economies were devastated by the rise in interest rates that began in 1978, and became extreme under Paul Volcker's late-1979 program of "controlled disintegration of the world

TABLE 2-4

### Looting through interest overcharges, various countries 1978-85

(billions of dollars)

	Interest paid (1)	Interest calculated at 6.8% (2)	Interest overcharges (1-2)
Argentina	28.9	16.8	12.1
Brazil	70.8	37.6	33.2
Colombia	6.8	3.8	3.0
Chile	12.4	6.1	6.3
Mexico	62.6	33.1	29.5
Peru	7.6	5.4	2.2
Venezuela	25.0	14.7	10.3
Ibero-America	<b>237.2</b>	<b>126.2</b>	<b>111.0</b>

Sources: Economic Commission for Latin America (U.N.) and authors' estimates.

economy." The effect of this increase in interest rates is calculated for Ibero-America in Table 2-3. This table shows total debt, total interest actually paid, the implicit interest rate (that year's interest payment as a percentage of that year's total debt), and what interest payments would have totaled at a constant 6.8% rate (the interest rate in 1977). At this rate of interest, a yearly overcharge can be calculated as the difference between the 6.8% interest rate and the actually prevailing rate. The next line shows the cumulative saving, which by 1985 totaled \$111.0 billion, almost one-third of the total debt. In other words, if interest had remained constant at 1977 levels, Ibero-America would today have \$111.0 billion less in foreign debt, or a total of \$259.0 billion, as indicated in Figure 2-2 above. Interest-rate looting thus accounts for about 30% of the official foreign debt.

Table 2-4 shows a breakdown of this interest-rate looting for the principal nations of Ibero-America.

**2) The terms-of-trade factor.** The second source of illegitimate debt accrual is the sharp decline in terms of trade experienced by the majority of the Ibero-American countries; that is, the difference between the inflation rates on prices paid for imports and those received for exports. In most of these countries, import prices rose while exports stagnated. For Venezuela and Mexico, the 1979 oil price increase made their terms of trade strongly positive, and made Peru's neutral. But despite such countervailing effects in individual cases, the balance for the entire continent was strongly negative.

Table 2-5 shows the effect on indebtedness that neutral terms of trade since 1977 would have had on the major countries. This was calculated by deflating both imports and exports by their respective unit value indices, reflatting them by the average inflation of world trade, and comparing this hypothetical balance of trade with the real one. The difference was the loss (or benefit, for Mexico and Venezuela) of trade revenues from this cause. As can be seen, Brazil, the largest economy, highly dependent on imported oil,

TABLE 2-5

### Looting of Ibero-America through deterioration in the terms of trade 1978-85

(billions of dollars)

	Official trade balance (1)	Trade balance with terms of trade of 1977 (2)	Net effect of the variations in the terms of trade (1-2)
Argentina	19.2	22.5	3.5
Brazil	17.2	118.4	91.2
Colombia	-8.5	9.5	18.0
Chile	-1.9	6.8	8.7
Mexico	29.9	12.9	-17.0
Peru	4.1	3.6	-0.5
Venezuela	45.1	13.9	-31.2
<b>Ibero-America</b>	<b>108.5</b>	<b>204.3</b>	<b>95.8</b>

Sources: ECLA and authors' estimates.

would have earned an additional \$91.1 billion, Chile \$8.7 billion, and Colombia \$18.0 billion. While the high relative cost of imported oil accounts for part of Brazil's high figure, falling prices for non-oil exports of all the countries was an equally significant factor, as shown by Colombia, which did not import oil, yet suffered proportionally even more than Brazil.

For the continent as a whole, \$95.8 billion was lost due to deteriorating terms of trade. Had that amount been applied to reducing the debt, it would have dropped down a second notch from \$259.0 billion to about \$163.2 billion (Figure 2-2). Terms-of-trade looting thus accounts for about 26% of the official foreign debt.

3) **The flight capital factor.** The third element, flight capital, was calculated much more conservatively than in a recent Economics Commission for Latin America (ECLA)

study, which estimates total capital flight from 1978-85 at \$160 billion. All of the "errors and omissions" category in balance-of-payments figures, and 60% of the "nonregistered" increase in yearly indebtedness, were added together to total flight capital. The close correlation between the years in which this combined total grew, and in which flight capital is known to have been at its height, confirms the validity of this measure, however approximate. Both categories showed large increases in the critical years 1982 and 1983, when capital flight is known to have been greatest. This conservative estimate places the 1977-85 total at \$89.5 billion.

Thus, if capital flight had not been induced, the foreign debt would have dropped by another \$89.5 billion to the modest sum of \$73.7 billion (Figure 2-2). This category of financial extraction thus accounts for about 24% of the official foreign debt.

4) **The interest on illegitimate debt factor.** Finally, there is a fourth category of loss: interest paid on the illegitimate portions of the debt, that is, the debts incurred to cover the deterioration of the terms of trade and flight capital. This totaled \$53.2 billion over the same period, or about 14% of the total foreign debt. Had it not been incurred, the total legitimate foreign debt of Ibero-America would have dropped to \$20.5 billion by the end of 1985.

In other words, the combined total of illegitimate debt comes to \$349.5 billion. Given that at the end of 1985, the total foreign debt officially reached \$370 billion, the *legitimate* foreign debt only reached a total of \$20.5 billion, about 5% of the illegitimate debt the banks claim they are owed! The other 95% has, by all standards of economic reality and equity, been long since paid off.

Table 2-6 is a summary of the relevant statistical documentation of this point, from which Figure 2-2 was drawn.

TABLE 2-6

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(billions of dollars)

	1978	1979	1980	1981	1982	1983	1984	1985	Total
1. Total official debt	156.5	183.9	226.4	282.7	322.8	343.7	361.4	370.0	
2. Increase in official debt									
	30.9	27.5	42.5	56.3	40.1	20.9	17.7	8.6	244.5
3. Interest rate overcharges	0.9	4.2	9.4	17.5	21.5	17.4	22.4	17.9	111.0
4. Terms-of-trade losses									
	7.2	5.6	3.2	13.0	18.1	18.5	14.7	16.6	95.8
5. Capital flight	4.9	1.5	14.0	20.4	24.1	14.0	5.8	4.8	89.5
6. Interest on illegitimate debt									
	0.1	0.9	1.9	4.1	7.2	10.3	13.1	15.5	53.2
7. Increase in illegitimate debt (3+4+5+6)	12.0	12.2	28.4	55.1	70.8	60.2	56.1	54.7	349.5
8. Increase in legitimate debt* (2-7)	18.9	15.3	14.1	1.2	-30.7	-39.3	-38.4	-46.2	-105.0
9. Total legitimate debt	144.4	159.7	173.8	175.0	144.3	105.0	66.6	20.5	

\*The negative figures indicate that the debt is being canceled.

Sources: ECLA and authors' estimates.

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