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1987 debt crisis in review: Bankers break Brazil's moratorium

by Peter Rush

On Feb. 20, 1987, the international banking community's worst nightmare seemed about to occur: the formation of a debtors' cartel to demand broad debt relief for Third World nations and force an overhaul of the world monetary system. Brazil's announcement came less than a month after the Vatican's Justitia et Pax Commission document condemning the dolorous impact on developing countries of servicing exorbitant debts. Given the influence of the Schiller Institute's campaign for an Ibero-American common market, Brazil's moratorium threatened to crystalize support from the rest of Ibero-America for a generalized moratorium.

While the bankers had been able to largely weather the effect of Peru's unilateral reduction of payments in 1985, by politically and economically isolating that country, the enormous relative weight of Brazil's economy—the largest by far in the continent—and of its debt—at $108 billion, the largest in the Third World—was altogether different. It meant that, had just one of Ibero-America's other two largest debtors, Mexico and Argentina, joined Brazil, the momentum to establish the cartel and common market would have become unstoppable.

For that reason, from Feb. 20 on, the State Department and Wall Street joined forces to bring Brazil's moratorium to a quick end, and politically eliminate its author, Brazilian Finance Minister Dilson Funaro. They achieved the latter goal within a little over two months, and the former in November, when Funaro's successor, Luiz Carlos Bresser Pereira, signed an agreement with the banks resuming debt payments. The April 26 sacking of Funaro broke the political momentum toward continent-wide action, and since that date, the continent has steadily lost ground in its battle for economic recovery and development.

By the end of 1987, the debt situation threatened to again become unstuck, as Argentina and Mexico both entered hyperinflationary stages, in the wake of the worldwide October financial crash and their own internal financial crises. Brazil was not far behind. The financial disintegration of the major nations of Ibero-America is on the agenda for 1988, if debt moratoria and integration are not adopted soon.

Unlike the debt crisis of 1982, this time the populations have already been looted to the limit, and the governments are indebted internally as well as externally to the point of bankruptcy. They cannot just repeat their 1982 austerity prescriptions. The November summit in Acapulco, Mexico, of heads of state of eight Ibero-American nations, set up the framework in which a joint response could emerge, by agreeing to regular consultation on such matters as foreign debt.

The Vatican paves the way

On Jan. 29, the Pontifical Commission Justitia et Pax published a document entitled, "At the Service of the Human Community: An Ethical Approach to the International Debt Question," which had been commissioned by Pope John Paul II after several trips to Ibero-America and Africa, where he had witnessed the destruction wrought by International Monetary Fund debt policies. In his "Presentation," commission chairman Roger Cardinal Etchegaray hit the IMF et al., saying, "When credit agencies consider the situation solely from the economic and monetary angle, they often impose on the debtor countries terms . . . that can contribute . . . to unemployment, recession, and a drastic reduction of the standard of living. This causes suffering, first of all for the poorest. . . . In brief, it is a situation that is intolerable, and, in the medium term, disastrous for the creditors themselves."

Stating what is developed as the major theme of the 30-page document, he wrote, "Debt servicing cannot be met at the price of the asphyxiation of a country's economy, and no government can morally demand of its people privations incompatible with human dignity." This last point, that morally, no nation can be compelled to destroy its economy and make its people suffer, just to pay debts, subsequently became the rallying cry across the continent, from Alan García's Peru to Acapulco, Mexico during the November heads-of-state summit there.

In a speech delivered April 6 during his trip to Argentina, Pope John Paul II reiterated the same theme, calling for "an ethical judgment of the international debt," and adding that the most radical threat to peace stems from "the foreign debt of many developing countries."

On Feb. 20, Brazil's President José Sarney promulgated the proposal of his finance minister, Dilson Funaro, and declared a unilateral moratorium on payment on the country's $67 billion owed to private banks. As outlined by Funaro over the succeeding two months, the moratorium had the potential to spark a continent-wide resistance. He repeatedly specified: 1) that the developed countries must recognize that the debt is a political question; 2) that tortuous, dragged-out negotiating processes must be ended; 3) that the issue is the

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Office of the President of Mexico

Eight heads of state met in Acapulco last November and set up the framework in which a joint response to the debt problem could emerge in 1988.

net outflow of capital—the outflow must be drastically reduced, if not eliminated; 4) that economic growth and improvement of living standards cannot be sacrificed in any debt payment arrangement; 5) that national sovereignty cannot be compromised, and that the IMF has no role in monitoring the economy or in any other capacity. In his Feb. 20 announcement, Sarney said, "Pope John Paul II was very clear. . . . He said that the problem of the foreign debt is also an ethical problem. . . . Indebtedness must not harm the basic living needs of a people," and, "We are suspending our debt payments. . . . We cannot pay the debt if it means the hunger of our people."

The announcement of the moratorium hit like a bombshell. Not since Mexican President José Lopez Portillo, following advice from Lyndon LaRouche, had nationalized the banks and adopted other emergency measures in September 1982, had there been a similar challenge to the IMF and the banks. The *Financial Times* of London summed up the bankers' panic in a Feb. 20 editorial entitled, "Brazil Succumbs to Populism," saying, "If Brazil does take unilateral action on debt servicing, the ramifications could be far-reaching. . . . An effective moratorium in Brazil would further unsettle banks and raise the specter of similar measures by other debtors." Press commentaries around the world echoed the same fears. Argentina, Venezuela, and Mexico were then in difficult negotiations over refinancing their respective debts.

Finally finding an ally for Peru in its heretofore isolated defiance of the IMF, and understanding the same dynamic that petrified the banks, Peru's President García immediately arranged to travel to Mexico in an effort to bring that country in on the side of Brazil. He made a triumphal visit to Mexico March 23-25, during which he captivated the population and won over the Congress, which he addressed in a speech that brought tears to the eyes of many congressmen. He invoked the Mexican Revolution, stating, "I refuse to feel that they can make us submit," and concluded with the appeal, "Let us speak the same language . . . and we are going to rip the cobwebs and break the paper tigers that scare some people." He left the hall to a standing ovation of legislators shouting "Bravo" and "Viva." However, the government of President Miguel de la Madrid remained impassive and did nothing, nor did Argentina, to help Brazil, thereby betraying it, leaving it in untenable isolation.

Shortly after García returned to Peru, and as the Pope was visiting Argentina, Lyndon LaRouche visited Peru for five days of meetings and conferences to support President García. From April 3-7, LaRouche met informally with congressmen, senators, leaders of various political parties, and leaders of other national institutions. He addressed 80 military officers and civilians at the Center for Military Studies (CAEM), and 400 attendees at a Schiller Institute-organized public forum, which received significant press coverage. He strongly backed García's efforts to force a new international approach to the debt and laid out the imperative for continental unity in a common market.

Counterattack

The specter of LaRouche teamed up with García, together with the Vatican, backing the Brazilian debt moratorium administered by Dilson Funaro, brought a swift counterattack

by the IMF, the U. S. administration, and monetarist forces within a number of countries.

In Peru, the very day that LaRouche arrived, a military coup attempt was carried out. It failed in its maximum objective of toppling García, but succeeded in preventing a scheduled meeting between García and LaRouche. García referred to that coup attempt in an interview in a Mexican newspaper on Dec. 17, saying that the presidential palace had been buzzed by Peruvian Air Force planes, and that he had been advised to flee, but had held firm and called the coup-makers' bluff.

That attack became the first of a series of actions against García that have, as of the present moment, seriously weakened his position. Next came a police strike in Lima May 15-18. The strikers threatened the presidential palace and were just barely contained. It was followed a day later by an communist-led general strike that, had it overlapped with the police strike, could have produced a social explosion. Immediately following that, the "Mexico" treatment was initiated. Flight capital accelerated and extreme pressure was put on the national currency, the inti, in the drug-money-fed black market for dollars.

In answer, on July 28, García counterattacked by nationalizing the major Lima banks, with several objectives: to stop capital flight and eliminate the dollar black market; smash the drug-money-laundering operations of several of those banks based in the Peruvian jungle areas; take away the primary power base of a financial oligarchy of a handful of families undermining his nationalist attempts to develop the economy; and democratize credit, making it available to medium-sized and small businesses and cultivators in all parts of the country.

The response was immediate and partially successful. Rallying behind the standard of the Institute for Liberty and Democracy and its leaders, Hernando de Soto and writer Mario Vargas Llosa, the financial oligarchy orchestrated a mass campaign appealing mainly to the middle class and business sector, with the lie that García's next target would be the rest of private business. While the bank nationalization bill was eventually passed by Congress in a modified form, the effect of the long, drawn-out battle, and of treachery from within his own APRA party, was to undermine the positive effects of the nationalization, and weaken García.

In October and November, capital flight was renewed. The new pressures on the inti forced a sharp currency devaluation in December. García capitulated and not only went along with the measure, which will hurt the economy, but also told the Peruvian population that it was a good measure, rather than explaining that it was a bad, but inevitable, step backward in light of Peru's isolation.

Even as operations against García were under way, the undermining of Funaro's position in Brazil was also advancing. Beginning within days of the announcement of the moratorium, Brazil's neighbors, Argentina and Venezuela, plus Mexico, all received or were promised generous debt refinancing packages to ensure that they wouldn't back Brazil. Then, on April 7, the day that LaRouche left Lima, U.S. State Department Brazil desk officer Elkin Taylor held "an intensive schedule of meetings" with Brazilian government and business leaders, to lobby against Funaro and the moratorium. The next day, Sao Paulo governor Orestes Quercia, apparently on cue from Taylor, demanded publicly that Sarney fire Funaro immediately—despite strong support for Funaro from the majority PMDB party and the vast majority of state governors. That same day, Sarney's international affairs adviser, Rubens Ricupero, whom Taylor had met with the day before, gave *Veja* magazine an interview demanding Funaro's replacement by a minister "with good contacts with the bankers."

This pressure, combined with the rise of inflation, finally led Sarney to capitulate and request Funaro's resignation April 26. His replacement, Luiz Carlos Bresser Pereira, while pretending at first to favor the moratorium, began systematically undoing Funaro's policy and preparing for an end to the moratorium. Brazil cut domestic consumption and increased exports to be able to pay more debt service. And he began an orchestrated dance with the connivance of U.S. Treasury Secretary James Baker and Fed chairman Alan Greenspan, which culminated in the November capitulation of Brazil to U.S. demands that the moratorium be ended, under the empty threat of being declared "value-impaired."

Reality intervenes: the financial collapse

But 1987 is not 1982. The same policies aren't working, and can't. First into the barrel went Argentina. Over the summer, its inflation hit a monthly 13% in August, accelerating a decline in wages and general economic disintegration that led to a Peronist sweep of the Sept. 6 elections against the governing Radical Party. After the elections, with no change in economic policy, inflation soared to 20-30% in October, while the public sector deficit widened and the reserves shrank toward zero. Hours before Brazil capitulated on its debt moratorium, Argentine Treasury Secretary Brodersohn visited Brazil, reportedly to offer a joint moratorium. This threat was sufficient to force the IMF to release its next disbursement, which will permit Argentina to avoid default into early 1988, but it is now widely predicted that Argentina will simply run out of money very soon and be in de facto moratorium, declared or not.

Mexico, the "model" debtor on the continent, became in two short months the "model" of hyperinflationary blowout. As early as mid-May, a group of international consultants headed by economist Julio Millan identified the Mexican stock market as a government-created bubble destined to burst. Five years of devaluations, cuts in real wages, and growing budget deficits that only worsened inflation, made the stock market and usurious government treasury bills the sole recipients of investment funds. The resulting flood of speculative capital into the stock market pushed it from 15,000 in early 1986 to 120,000 in May 1987, to 375,000 by Oct.

9—whence it began its vertiginous 75% descent back to 110,000 in two short months—in pesos worth only 60% of their May value.

As identified by *EIR* columnist Carlos Cota Meza on May 29, the policy that brought about the crash was the work of central bank head Miguel Mancera and Agustín Legorreta, owner of the second largest brokerage in Mexico and head of the Businessmen's Coordinating Council, on behalf of the financial oligarchy who were playing to buy the next President of Mexico. With the selection by de la Madrid of Salinas de Gortari a scant five days before the crash, the oligarchy had its man as the presumptive next President of the country.

But it was the global stock market crash beginning Oct. 6, with a relative culmination on Oct. 19, that sealed Mexico's financial doom—and insures similar crises throughout the continent in the near future. Following Oct. 19, a chain reaction of capital flight and drain of reserves was set off that reportedly emptied at least $2 billion out of Mexico's reserves, in less than two months, until the central bank suspended its support for the free market peso on Nov. 19. The peso promptly plummeted by about 50%. But that move in turn led to 50% overnight price hikes in many parts of the economy, for which the labor movement demanded compensation.

De la Madrid issued a statement warning of the danger of hyperinflation. Ostensibly to forestall this eventuality, de la Madrid suddenly opted for an orthodox austerity program so severe that a 10% decline of the GNP is officially forecast for the first quarter of 1988, brought on by price hikes of 85% in gasoline and electricity, 100% in public transport, and 15-50% in food staples, including tortillas, bread, and milk. Mass layoffs began, with 150,000 government bureaucrats. No one outside of de la Madrid's coterie of financial confidants expects anything but increasing chaos and crisis under this policy.

Five years of IMF prescriptions to increase exports and slash imports, have devastated the Ibero-American continent's physical economy. After five years, inflation is 145-170% in Mexico, and over 300% in Brazil. In Argentina, it hit an 800% annual rate in October. Mexican wages, in real terms, fell 57% between 1982 and July 1987, according to one study, and by 46% between January and October of 1987 alone, according to another—and they fell dramatically again after the Dec. 8 price hikes. As of May 1987, Argentine industrial salaries were only 57% of their 1976 levels, and they have fallen substantially since then. The minimum wage in Brazil has fallen from $90 in 1981 to $65 in January 1987, to $40 by November—and 42% of families earn less than the minimum wage.

The health and nutritional levels of the population have collapsed. Story after story has appeared in the Mexican press documenting the extent of malnutrition of children, causing permanent brain damage, and of preventable, poverty-related diseases and child mortality. Unemployment is calculated by the Mexican Labor Congress to be 32%. In Brazil, 90.8 million people, 67% of all Brazilians, cannot obtain the minimum figure of 2,250 calories, and 36 million children are malnourished. In the Northeast, the average intake is only 1,845 calories, and 86.5% of children under 5 are malnourished, a study reports. Even in food-rich Argentina, the quality of the population's diet is declining fast. Over the past five years, 17,000 small and medium-sized industries have folded, 200,000 manufacturing jobs have disappeared, and manufacturing GNP has fallen 18%.

While real production collapses, governments have slashed investment budgets and cut services, but continued ballooning debt service payments. About 55% of Mexico's 1988 projected budget is to pay debt service, some 33% of the entire Gross National Product. Brazil's budget deficit is also above 30% of its GNP. Argentina promised the IMF it would reduce its deficit from 8% of GNP to 4%, after which government revenues dropped 20%. All three countries face a near-term drastic worsening of their deficits, as projected revenues fail to materialize because of falling economic activity, threatening hyperinflation, and bankruptcy of the state.

Toward 1988: 'Operation Juárez,' or bust

Everything that LaRouche told Ibero-American leaders back in 1982, and repeated since then, has come true. In September of 1986, the Schiller Institute published a book in Spanish, *Ibero-American Integration: 100 Million New Jobs by the Year 2000!* which elaborated in detail the required programs of physical integration, great infrastructure projects, common market mechanisms, and monetary measures, required to implement the 1982 "Operation Juárez" proposals. Beginning in fall 1986 and continuing through 1987, forums and seminars on the book were held in Mexico, Brazil, Argentina, Peru, Colombia, Venezuela, Bolivia, the Dominican Republic, Honduras, and Guatemala. Top economic planners and military and political figures attended these meetings, and indicated their intention to fight for the policy perspective outlined. As a result, today, LaRouche's "Operation Juárez" approach as spelled out in the *Ibero-American Integration* book is hegemonic within anti-monetarist circles throughout the continent, and is universally recognized as the only alternative to continuing economic and financial disaster.

The close of 1987 saw several developments that point to the possibility that 1988 could be the year that the continent finally unites to fight back along the lines laid out by LaRouche and the Vatican.

Two and a half years after García first proposed it, the eight members of the Contadora Group and its support group—Mexico, Colombia, Panama, Venezuela, Brazil, Argentina, Peru, and Uruguay—met in Acapulco Nov. 24-28 for a first-ever summit. The most important agenda item was the growing debt crisis. While not agreeing on any specific course of action—as García had urged—the Presidents did make their strongest-yet affirmations of the necessity to reduce debt payments in accord with the ability of each country pay—