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Financial mudslide is spreading beyond Mexico

by Valerie Rush

Panic spread through financial centers around the world on Jan. 9, when the billions of dollars—and pledges of billions more—that were poured into financially bankrupt Mexico failed to reinflate the speculative bubble upon which the myth of the "Mexican miracle" has rested for the past decade. The country's stock market meltdown, coming on top of the peso's plunge, has since been followed by a slow-motion collapse of the banking system. Similar scenarios are beginning to unfold in virtually every part of the world, as it becomes evident that this is a crisis not just of Mexico, but of the entire international financial system.

In Canada, the other partner of the United States in the doomed North American Free Trade Agreement (NAFTA), the currency hit a nine-year low, despite central bank intervention, while analysts point nervously to Canada's $540 billion foreign debt liabilities, expected to double by 1998. These were incurred, like those of Mexico, to finance the nation's trade deficits in recent years. Countries as diverse as South Africa and Indonesia are issuing statements denying that they have Mexico-style currency and debt troubles. In Europe, as of mid-January, the devastation was spreading from country to country:

- In **Italy,** saddled with a $1.2 trillion debt ($60 billion of which is due in January alone), the lira is in free fall, triggered by a full-scale government crisis. With $120 billion in foreign money invested in its stocks and bonds, Italy could face capital flight rivaling Mexico's at a moment's notice.
- In **Sweden,** the U.S. credit agency Moodys has downgraded the debt rating, citing an out-of-control budget deficit and public debt of more than 90% of Gross National Product.
- The financial crisis in **Spain** has caused the peseta to plunge below the floor limits of the European Monetary System's currency band. Capital flight and an official unemployment rate of over 18% has heightened the instability.
- In **France,** already burdened by a huge budget deficit and soaring unemployment, the state is having to pump some $5 billion into the giant Crédit Lyonnais bank to keep it from going under.

Most dramatically affected are Ibero-America's other "showcase models" of liberal free-trade economics, such as Argentina, Peru, and Brazil, where bank collapses, capital flight, and stock market crises are dominating the headlines. Also suddenly in the headlines are U.S. economist Lyndon LaRouche and his 19th-century predecessor, German-American economist Friedrich List, whose principles of physical economy (known as "the American System") are diametrically opposed to Adam Smith's free-market prescriptions, whose consequences are today in evidence for all to see.

LaRouche was right

In June 1994, LaRouche issued his "Ninth Forecast," foreseeing a crash of the financial markets and the unraveling of the world monetary system (see *EIR,* June 24, 1994). He warned goverments to get off the *Titanic* and onto the lifeboats while there was still time. In most cases, LaRouche's warnings have not been heeded. The problem is that the financial whiz-kids who are running the banks, the stock markets, and the governments in many parts of the world are refusing to believe that what's going on is a disintegration of the international financial system to which they've pledged their allegiance. They still think they can manage their way out of the crisis. So, instead of abandoning the sinking *Titanic,* they are drilling holes in it to try to drain it.

Washington's response to the Mexico crisis is an example. Under intense pressure from Wall Street and the bankers who run the U.S. Federal Reserve, President Clinton has offered to put together a package of loan guarantees of $30-40 billion for bankrupt Mexico, effectively pledging the U.S.

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Treasury as collateral. The money is not for Mexico, however. It will go to the Wall Street and City of London parasites who are killing their Mexican host, and as a result are now dying themselves. But not even the U.S. Treasury can bail out a world financial system that is going belly up.

Foolishly, Mexican President Ernesto Zedillo has responded to the crisis with measures that can only exacerbate it. He has put virtually the entire Mexican economy up for sale—with the "plum" of Mexico's oil apparently being kept in reserve as a last resort—and has unveiled a wage-gouging policy which makes *EIR*'s May 1991 prediction of an "Auschwitz south of the border" frighteningly accurate. In the face of *official* forecasts of 19% inflation for 1995—a forecast already being laughed at as absurdly low by world financial experts—Mexican workers have been offered a 4% wage increase for the entire year, along with an "optional" 3% supplement in the form of so-called productivity bonds!

On Jan. 11, it was announced that prices on some 80 items of the "market basket" of commonly consumed goods would be allowed to rise to compensate for the impact of the peso devaluation on "imported components." The consequence? The next morning, Mexicans woke up to stunning price increases of 30-40%. Many Mexicans are now wondering how long they will be able to keep up the mortgage payments on their homes; others are wondering how long their jobs will last; still others are wondering how much longer they can feed their families.

How long Mexicans will put up with the murderous austerity and the "fire sale" of Mexican patrimony remains to be seen. Pressures are already being applied to get President Zedillo to attempt a *La Quinazo,* supposedly to "restore his credibility." The reference is to former President Carlos Salinas's decision early in his administration to send in the Army to arrest Mexican oil workers' union president Joaquín Hernández Galicia (known as "La Quina"), a politically influential figure who was an important obstacle to Mexico's entrance into George Bush's NAFTA. "La Quina" has just finished his sixth year in prison. Zedillo is resisting these pressures, but growing labor discontent over his newest austerity measures could change that.

Despite the fact that on Jan. 9 the Mexican government drew on the $18 billion emergency credit line set up by its NAFTA partners and others, and despite an unprecedented intervention by the U.S. Federal Reserve Bank into the foreign exchange markets to buy up pesos, the speculative capital that has poured into Mexico by the billions in recent years continued to flee the country at record rates. On Jan. 10, the peso plunged to nearly 6 pesos to the dollar, compared to 3.4 pesos less than a month previously. Simultaneously, Mexico's foreign reserves were revealed to have sunk to an unacceptable $5.5 billion, equivalent to just one month's worth of imports. That day, U.S. brokers began telling their clients to "get out of Mexico, no matter what losses you incur."

Desperate government efforts to pull dollars back into the country included hiking interest rates on short-term treasury notes (*Cetes*) to a whopping 50%, which translated into a similar increase in interest rates on overnight (interbank) loans. Consumer loans are expected to follow suit. The immediate consequence was a stock market meltdown, as "investors" fled into the more lucrative government paper, and a more generalized banking panic as the prospect of new waves of consumer and business defaults on top of already unmanageable debt arrears hit home.

At the same time, foreign holders of certificates of deposit (CDs) in Mexico's banks—which account for some $8 billion in Mexican bank debt—began to cash in their CDs, forcing the dollar-strapped banks to turn to Fobaproa (the Mexican equivalent of the U.S. Federal Deposit Insurance Corp.), which has in turn wrung a promise from the government to fork over more dollars for its bailout fund. At the same time, of course, the government is being forced to turn to the U.S. and Canadian treasuries to come up with dollars to pay off maturing dollar-denominated treasury notes known as *tesobonos,* $18 billion of which are in the hands of very nervous foreigners.

'The tequila effect'

A string of crises has broken out elsewhere on the continent, and has been dubbed "the tequila effect" by the Ibero-American press. Most striking is the case of Argentina, whose President Carlos Menem was still bragging about a month ago, "We've done everything Mexico has done, only faster." Today, with its own stock market in crisis, interest rates soaring, and a banking system which has started to go under, Finance Minister Domingo Cavallo is monotonously repeating, "Argentina is not Mexico."

A $200 million "safety net" set up in early January by five major Argentine banks to help out smaller banks with "liquidity problems" began to fall apart almost immediately when depositors began pulling dollars out of the system, to the tune of $20 million a day, despite a one-to-one parity with the Argentine peso. On Jan. 9, Central Bank head Roque Fernández reported that today there are more than ten banks which have turned to the safety net, "and the number will grow." Cavallo himself went off to New York, armed with charts and graphs to convince investors and bankers of Argentina's solvency and to announce, "We're going to sell whatever is still left," as the Buenos Aires daily *Clarín* headlined its coverage of his trip.

Brazil was similarly described as highly vulnerable to the "tequila effect" by former Finance Minister Antônio Delfim Netto, in an article published in the Jan. 9 *Gazeta Mercantil.* Delfim Netto referred to the volatile nature of $25 billion in foreign-held short-term government debt and another $15 billion in foreign stock holdings—in combination, the equivalent of Brazil's $38.7 billion (and falling) foreign reserves—combined with what he called a 30% overvaluation of the Brazilian currency, the *real.* Delfim Netto urged a currency devaluation as the answer. The government's "solution" has been to sell more than $2.65 billion worth of dollar-denominated debt titles, called NTN-Ds (the equivalent of Mexican *tesobonos*), in 17 days, reportedly at the suggestion of the International Monetary Fund and the U.S. Federal Reserve, as a way to signal the market that Brazil isn't planning to devalue the *real*.

Looking to Friedrich List

Although many governments still blindly insist that the Mexico "storm" will soon blow over, others are beginning to decipher the handwriting on the wall. The spate of articles that has appeared internationally on 19th-century "American System" economist Friedrich List suggest that some are beginning to look for alternatives. On Jan. 7, for example, the *International Herald Tribune* ran an article by U.S. commentator William Pfaff, who attacks the "religions of markets" for sacrificing people to "speculative advantage," and promotes the Listian policy followed by the Asian "economic miracles" and by the American economy in the 19th century.

List has also been promoted in the press in Venezuela, a country which has thus far escaped the worst of the "tequila effect," thanks to exchange controls imposed last year after its own speculation-riddled banking system collapsed. On Jan. 9, widely read economics columnist Alfredo Schell wrote in *El Universal* that List's books "are being dusted off" by many who are "participating in the debate beween liberalism and interventionism, including in the United States of America." Schell wrote that Venezuelan President Rafael Caldera, although "not an economist, has—unlike what many people opine—a definite and clear conception, a doctrinaire vision of the focus that should be given the economic issue." That focus, suggests Schell, is based on "the rational and up-to-date identification of the President with the instructive lessons of List."

The "instructive lessons of List" are being echoed by members of the Venezuelan diplomatic corps, to judge from the comments of Venezuelan Ambassador to Brazil Alfredo Toro Hardy, who wrote in a Jan. 5 article in the Caracas daily *El Universal* that the lesson of Mexico is that "the dictatorship of the stock market has failed." Wrote Hardy, "The policies of countries are priced in the stock markets as if they were corporate stock. . . . The great decisions of a country in effect now depend less on national projects or goals than on what Wall Street 'traders' say in their reports." Hardy contrasted this approach to the German and Japanese models, which used the great national banks to provide capital for industry, for research, and for building up human resources as the means to improve technology and increase productivity.

Media spotlight on LaRouche's forecasts

Since the devaluation of the Mexican peso on Dec. 20, the views of American economist Lyndon LaRouche—who forecast just such an international financial crisis and designed proposals to revitalize the physical economy—have been getting increased attention in Ibero-America. Following is a sample of some of the recent coverage.

"Economist LaRouche Forecasts 'Foreseeable' Collapse of World's Financial System," headlined the Jan. 9 issue of the western edition of Mexico's business daily *El Financiero*.

"Crisis of Financial System Was Forecast by Controversial American Economist Lyndon LaRouche," headlined the Peruvian daily *Correo* on Dec. 31.

"Argentina Is Next," headlined the Argentine newspaper *Punto Critico* on Jan. 6. The coverage was based on statements made by LaRouche in a radio interview on Dec. 28, during which he also said that the crisis "is not a Mexico problem, it is a Wall Street problem." The statement was also covered by Peru's leading opposition daily *La Republica* on Jan. 2 and by the business newspaper *El Inversionista* on Jan. 9. It also received radio and TV coverage, including on Jan. 2 on "Encounter with the Truth," hosted by Julio Ortega on Panama's Radio Metropolis, and on Jan. 3 on Channel 2 in the Dominican Republic.

"Mexico Needs an About-Face in its Economic Policies: Debt Moratorium and Exchange Controls," headlined the Jan. 5 issue of the daily *Ultimas Noticias* of Venezuela, reporting on a statement issued on Dec. 28 by the Mexican branch of the Ibero-American Solidarity Movement (MSIA), which includes many LaRouche collaborators.

The Mexican crisis is a symptom of "the collapse of the system, a symptom of the collapse of the philosophy of Milton Friedman and Newt Gingrich," said LaRouche in a Jan. 4 radio interview with "*EIR* Talks," which was covered by Argentina's *El Informador Publico* and *Punto Critico* on Jan. 13

"Stop the Bankers' Takeover of PEMEX; Stop the Takeover of Chiapas by the British Mercenaries of the EZLN," a second statement issued by MSIA on Jan. 7, was covered in the Jan. 11 issue of *Diario del Yaqui* of Sonora, Mexico, among other places.

"LaRouche Says NAFTA Is Dead," was the headline in the Jan. 13 issue of the Dominican Republic daily *El Nuevo Diario*.