

Monetarist corpse floats in Brazil

by Lorenzo Carrasco

The high tides caused by the crisis of the Asian financial markets failed to respect the dike of lies so carefully constructed by the government of Brazilian President Fernando Henrique Cardoso, and are now flooding Brazil, forcing to the surface the fragility of the monetarist deception in this country.

As in the case of South Korea, what we are seeing is a pyramid of very short-term debt, whose total quantity is unknown to the country's own monetary authorities. "Globalization" has in effect erased the main differences between foreign and internal debt, making a rigorous accounting of actual finances impossible.

This paper pyramid has three major components: 1) the runaway growth of public bonds; 2) the growth of private foreign debt, both in bonds and direct loans, with the aggravating factor that foreign banks recently established in Brazil are now also lending directly on the domestic market, using the resources of their branches; and 3) the relationship of the two previous components to the Brazilian derivatives markets.

According to the January 1998 issue of the Central Bank's newsletter, domestic debt through November 1998 is now equal to \$228 billion, of which nearly \$200 billion consists of public, federal, state, and municipal paper. The majority of these loans are renewed every 60 days. In the first trimester of 1998 alone, \$60 billion will come due, and will be renewed only with great difficulty, despite the recent steep rise in interest rates. The Brazilian government had to offer an annual interest rate of 37.76% on bonds it floated during the first week of 1998. Furthermore, nearly \$35 billion of the total debt is in the form of dollar-denominated National Treasury Notes (NTN-Ds).

The Central Bank also reports that, as of September 1997, the official foreign debt reached \$188.4 billion, of which \$100 billion is private sector debt. As commentator Aloysio Biondi stressed in his weekly column in the Jan. 9 *Folha de São Paulo*, both the government and private companies are facing enormous difficulty in renewing their credit abroad, and are only getting extremely short-term bridge loans.

The Bank for International Settlements in Switzerland states that Brazil had, until mid-1997, some \$71.1 billion

worth of accumulated debts with private creditors, of which 62.2%—that is, \$44.2 billion—are short term. But, according to the BIS, with the recent changes in banking legislation in the United States, the U.S. Treasury is no longer demanding that banks with branches in Brazil count as part of their international credits, those dollars loaned to Brazilian companies through their branches. The BIS estimates that, as of June 1997, there was \$39.1 billion loaned to Brazil through the local subsidiaries of international banks, which are not included in calculations of the official foreign debt. Therefore, the BIS calculates that the total debt to private creditors is actually \$110 billion, and the foreign debt of the country on the order of \$230 billion.

Even so, to get a complete picture of Brazil's total real foreign debt, one must add to the BIS's own figure, the categories of other public bonds denominated in dollars (NTN-Ds), public bonds held by foreigners but denominated in *reales*, foreign investment in Brazil's stock markets, etc.

The third problem is the relation of all this debt to the Brazilian derivatives market, the fourth largest in the world, with a negotiated volume of nearly \$7 trillion in 1997. Here is where the real uncertainties emerge, because no one yet knows how much was lost by whom, with the sudden doubling of interest rates last October. According to the Jan. 5 *Wall Street Journal*, two months after the October crisis, no one knew how much Brazil's banks had lost. Even now, only \$800 million in losses are recognized. "Some of the derivative positions taken by Brazilian banking institutions still haven't closed, making a full accounting impossible," states the *Journal*. "If Brazil's attempt to defend the *real* fails and the country is forced to devalue the currency, then all bets are off for the banks."

Cardoso's strategy

Of course, the Cardoso government is planning to survive until next October's elections, in which the government expects to be a shoo-in, by virtue of continuing to implement the same prescription: maintaining the net flow of foreign speculative capital, by offering extremely high interest rates; privatizing all infrastructure companies; and looting the population through unemployment and low wages, while industry suffers a collapse.

But time is running out on this little game. First, the unpayable debts of the private sector reached \$60 billion by the end of 1997, equivalent to 23% of all private sector loans. This will increase dramatically in the first months of 1998, because of the higher interest rates. Secondly, because of those same interest rates, employment and industrial production will fall, which will lead to a drop in tax revenues, in turn increasing the deficit that the interest rates hikes were intended to combat. The result will be an increase in government debt, at a minimum rate of \$6-8 billion a month.

All that is needed is some additional commotion on the international markets, for the entire pyramid to collapse.