Peru's Fujimori must abandon the IMF, before it is too late

by Luis Vásquez Medina

In his two months in office, Peruvian Finance Minister Víctor Joy Way has been able to offer nothing but failure. The Fujimori government continues to underestimate the international financial crisis, mistakenly believing it to be temporary in nature. They continue to believe the foolish economist Carlos Boloña, who some time ago said that the crisis would only last 24 months. Thus, the government blindly continues to administer the same International Monetary Fund (IMF) medicine that has already killed many Peruvians.

Following each new blow of the crisis, which exacerbates the flight capital and adversely affects the exchange rate, Finance Minister Joy Way turns to what, it appears, is the only thing he knows how to do: contract the money supply in soles, Peru's currency, to impressive levels. This monetary austerity has produced an "overnight" interbank lending rate of 75%!

The resulting recession has grown very serious. Manufacturing fell 12.6% in February, compared to the same period a year ago; construction fell 9.7%, electricity 0.4%. Fishing and agriculture are the only sectors which have shown some recovery so far this year—a virtual "recovery," because the comparison is to the same period in 1998, when the effects of El Niño had practically eliminated these activities altogether.

It is currently estimated that tax arrears are between $7 and $7.5 billion, and businessmen have just demanded a new amnesty and consolidation of their tax debt. The collapse in consumption has reached unprecedented levels, and the National Society of Industries has stated that under current conditions, businesses are simply unable to meet their loan payments to the banks. The recession is also affecting imports; last February, customs tariffs collected fell 22% compared to the previous year, and in January had already fallen 5.3%.

What has Joy Way, whose adviser is Harvard economist Jeffrey Sachs, done to deal with this crisis? He has proposed a multimillion-dollar tourist project on San Lorenzo Island, to be financed by Las Vegas capital, which both Joy Way and Sachs know full well comes from the mafia of gambling casinos, prostitution, and drug trafficking.

Foreign looting

The so-called "macroeconomic bonanza" in which so many deluded businessmen still believe, and which even the opposition accepts, simply doesn't exist. Peru today, thanks to the economic destruction caused by the opposition party APRA's socialism and Fujimori's ultraliberalism, is very vulnerable to every international crisis. Its ability to produce internally, even the basics, has practically disappeared. Today, 70% of the average Peruvian's diet is imported, and the effects of a very likely run on the country's capital could be devastating.

TABLE 1
Peru: real foreign debt
(billions $)

	1996	1997	1998
1. Public*	26.3	19.7	19.8
2. Private			
a) non-financial companies	5.8	5.5	6.1
b) banks	1.7	3.3	4.3
3. **Official foreign debt (1+2)**	**33.8**	**28.5**	**30.2**
4. Foreign portfolio investment	3.2	4.0	2.8
5. Dollar-denominated domestic debt	ND	ND	5.5
6. **Real foreign debt (3+4+5)**	**37.0**	**32.5**	**38.8**

* including BCR
Source: Central Reserve Bank.

First of all, it is not true that Peru's foreign debt has been reduced, as Fujimori gleefully states. What has apparently fallen is only the *public* foreign debt. The debt of the public sector (see **Table 1**) in 1996 was calculated by creditors at $26.289 billion. After the Brady Plan, it was reduced in 1997 to $19.7 billion. However, what actually happened was that the figure was purposely inflated, followed by a supposed discount. Thus, although the public foreign debt has apparently fallen, as a consequence of financial deregulation (as in other countries on the continent), a new kind of foreign debt has begun to grow: the foreign debt of the private sector.

The business sector began to go into debt directly with foreign banks, issuing bonds abroad and even placing trading them on foreign stock exchanges. Also, private Peruvian banks began to loan abroad. The private foreign debt grew quickly: In 1996, it was $7.516 billion and by 1998, it had reached $10.394 billion. The problem with these loans is that they are very short term, and their conditions are very onerous. According to the New York-based Moody's rating service,

TABLE 2
Peru: foreign investment
(billions $)

	1996	1997	1998
Direct investment	6.6	7.5	7.7
Portfolio investment	3.2	4.0	2.8
Total	**9.8**	**11.5**	**10.5**

Source: Central Reserve Bank.

TABLE 3
Peru: capital export, 1998
(billions $)

Public foreign debt service	1.7
Private foreign debt service	1.5
Capital flight from the stock market	1.2
Total	**4.4**

TABLE 4
Peru: balance of payments
(billions $)

	1990	1995	1999
1. Goods	–0.3	–2.2	–2.5
2. Services	–0.5	–2.1	–1.3
Current account (1+2)	**–0.8**	**–4.3**	**–3.8**

Source: Central Reserve Bank.

TABLE 5
Peru: international reserves, 1999
(billions $)

1. Net international reserves	9.5
2. Bank deposits	3.2
3. Debt to the IMF	0.8
4. Illiquid	1.8
5. Available (1-2-3-4)	**4.0**

Source: Central Reserve Bank.

more than 75% of this debt, some $7.5 billion, is short term.

However, this is not all of Peru's real foreign debt. There is another, very volatile debt, which could be called in at any time—the famous "hot money," or foreign investment which has done so well betting in the Lima stock market (BVL) (see **Table 2**). In 1998, this amounted to $2.775 billion, $1.2 billion less than in 1997. The difference corresponds to capital flight which reveals the volatility of this kind of debt.

And lastly, to discover Peru's real degree of indebtedness, one must add in the internal debt that has been contracted in dollars with foreign banks or foreign financial entities which, given the deregulation, face virtually no restrictions in placing credits on the domestic market.

Here we include those dollar loans which a head of household takes out to buy school supplies for his children at the unfortunately well known "consumer banks," which are primarily Chilean. Also included are the dollar credit lines—which the population uses to buy appliances, cars, and houses—from foreign banks that operate in the country. That debt is conservatively estimated at some $5.5 billion for 1998. All this means a real foreign debt of nearly $39 billion.

So far in the Fujimori government, the country has paid more than $11.5 billion for foreign public debt service alone. In 1998, a year that proved extremely negative for the economy because of the El Niño phenomenon, the government paid out $1.67 billion. For 1999, President Fujimori himself has announced that Peru will pay $1.607 billion, since "the foreign crisis will not prevent us from continuing to meet our obligations."

But that's not all that went out in 1998. As **Table 3** shows, the total outflow of capital for 1998, from the stock market and for debt, was $4.391 billion.

Exchange controls, or catastrophe

Capital outflow, due to the necessity of purchasing ever larger quantities of merchandice and "services" (including interest payments and profits of direct foreign investment), as seen in **Table 4,** could not continue to be financed with new incoming foreign capital. The speculative capital that came in, attracted by inflated profits on the Lima Stock Exchange, is now leaving in a hurry. The capital that was going to flow into large mining and energy projects, on which the government has gambled the future of the country, is now not going to come. La Granja, Quellaveco, Camisea, and other projects have been cancelled. It has just been announced that funding for the last mining project, the $2 billion Antamina, will most likely not materialize, because there are no interested foreign investors.

Hence, in the future, the average annual current account deficit of $4 billion can no longer be financed, and the entire weight of the international crisis will fall on the national economy. These deficits meanwhile have begun to take a toll on the level of reserves and on the exchange rate. As seen in **Table 5,** these, in large part, are made up of reserve ratio and deposits in the Central Reserve Bank. The $4 billion available doesn't even cover seven months' worth of imports, and is less than the total capital that left the country in 1998.

So, given the liquidity needs of the international financial bubble, Peru's reserves could dry up in a matter of weeks, and the sacrifice of years will have been in vain. The government faces no other alternative but to follow Malaysia's example and to join the "Survivors' Club," decreeing exchange and capital controls.