Banking by Kathy Burdman

Loans only Volcker could love

The Fed chairman considers any bad Ibero-American debt good, if it's on Citibank's books.

Details are emerging on Federal Reserve chairman Paul Volcker's plan to rip up U.S. banking regulation on foreign debt. As *EIR* reported last week, Volcker intends to allow the money-center banks to accept interest payments on their dollar debt not in dollars, but in Brazilian cruzeiros, Mexican pesos, and other soft money.

Under U.S. law, loans whose interest is not paid in dollars for more than 90 days must be declared "nonperforming," and the bank must write off that interest income. Brazil is already 120 days in arrears in its $7 billion interest bill for fourth quarter 1983 and first quarter 1984. They will pay up to $4.5 billion of that in cruzeiros.

To cover up the fact that Brazil and other debtors are "just a tiny bit pregnant" with arrearages, Volcker invented a new bank regulators' category where any loan whose arrearages are inconvenient could be hidden.

This was revealed in an interview last week with a source close to Volcker, who gave the Fed chairman's interpretation of the Dec. 15, 1983 "Interagency Statement on Examination Treatment of International Loans," masterminded by Volcker and published by the Federal Reserve, the Treasury's Office of Comptroller of the Currency, and the Federal Deposit Insurance Corporation.

The Volcker Interagency Statement was bad enough. It rewrote the three regulators' category system for foreign loans. Previously, if a loan was "non-performing" (90 days in arrears), it usually was "classified" by the regulators, i.e., tagged as bad, under one of three categories: substandard, value-impaired, or loss.

The Interagency statement created a fourth category, "Non-Classified Credits Warranting Attention," consisting entirely of what will now be called Other Transfer Risk Problems (OTRPs). "This category applies when:

"1) A country is not complying with its external debt service obligations, as evidenced by arrearages, forced restructuring, or rollovers;

"However, the country is taking positive actions to restore debt service through economic adjustment measures, as part of an IMF program.

"2) A country is meeting its debt obligations, but non-compliance appears imminent;

"3) A country has been classified previously, but recent debt service performance indicates classification is no longer warranted. . . ."

According to my Fed source, Volcker crony Fed Governor Henry Wallich told a meeting of top New York bank executives at Citibank Feb. 12 that this means a debt can now be totally bankrupt as shown by "arrearages, forced restructuring, or rollovers," or about to be, or still be, and remain unclassified. "The regulators are willing to account the loans to be performing loans, and will not account them to be non-performing," Wallich said.

By what criterion is a loan granted this new treatment? The Fed's say-so, which the Interagency statement calls "*judgmental factors* in the general assessment" of the loan by the regulators.

In fact, the criterion is that to be overlooked, the debtor's bad debt simply has to be big enough and bad enough to bankrupt the monetary system. The Interagency Statement also makes plain that only the worst loans will be protected.

"The agencies recognize the importance to the stability of both the international banking system and world economy of providing continued international flows of bank credit, especially to countries implementing IMF-approved economic policies. Such new flows may strengthen the functioning of the adjustment process, help to improve the quality of outstanding credit," it states.

That is, my Fed source said, "We can't criticize loans to any big debtor like Mexico or Brazil, or it will cut off new credit and undermine the IMF's power!"

Wallich explained that these big debtors will be exempt from penalties now being slapped on the poorest Fourth World nations under Section 905(a) of the U.S. IMF bill, which he wrote. He interpreted for them the Fed's Dec. 23 document R 0498, which states that debtors who show "failure. . . to make full interest payments on external indebtedness" must have their loans classified as "value-impaired," and the loan principal written off.

Wallich told the bankers that exception would be made in the case of big debtors, such that "full interest payment" for these countries, to fullfill requirements of Sec. 905(a), need not be made in U.S. dollars. He told the bankers that they could accept cruzeiros as payments on all their Brazilian loans without time limit, and similarly with other big debtors.

"Can we account the cruzeiro interest as income?" he was asked. "You can account it any way you and your accountants wish," he answered.

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