Debt bomb set to blow up; hunger, disease spreading

by Peter Rush

Developments in the last few weeks in Argentina and Brazil suggest that both countries are very close to blowing apart financially, with Mexico not far behind. The near future holds the promise of wild gyrations of interest rates, steep devaluations, skyrocketing inflation, banking system collapse, and even national bankruptcy, not to mention the potential for popular explosions on the Venezuelan model which could dwarf that nation's ugly experience. At such a point, all bets will be off concerning each country's continued acquiescence to being looted by the International Monetary Fund, the banks, and their domestic enforcers, starting with the present presidential administrations in all three countries—exactly as has occurred with Venezuela's pro-IMF President Carlos Andrés Pérez.

The haughty refusal of the Bush administration even to throw the "big three" Latin American debtors a few crumbs on the debt issue, adds insult to the latest injury, the sharp rise in interest rates, which are now more than 3% higher than this time last year, and which will add $10 billion to the continent's interest payments due this year. This is occurring as interest rates in Argentina have hit 40% *a month*. People are fleeing from the austral into dollars, and the country has been unable to pay interest on its foreign debt since last April and is now $2 billion in arrears. Brazil, also hard hit, has just slashed wages, jacked the interest rate through the ceiling, and announced that it cannot pay its debt service due in March. And Mexico suddenly finds itself without its traditional trade surplus, and hence unable to pay its current interest, much less several billion dollars more, even as its agricultural sector is collapsing, and recession is deepening.

Simply put, the post-1982 measures adopted by the "big three" to pay $25 billion or more in annual tribute to the banks, have destroyed their economies. These measures depressed living standards sufficiently for the countries to run enormous trade surpluses with which to pay the debts, but at the cost of collapse in investment, stagnation or decline in total output, devastation of the health of the population, and a wrecking of internal financial stability such that each country now has stupendous *internal* debts, government budget deficits, extreme inflation, collapsed banking systems, and capital markets used for nothing but speculation.

For all of this, the debts of all three nations are 20% or more higher than six years ago, the interest burden greater than ever, and the ability to continue cutting living standards and investment is finished. Voters in Mexico and Brazil decisively voted against the governments that had imposed these policies in elections last year, and are likely to do so in Argentina this May. All three countries are reduced to playing hyperinflationary games to try to stave off financial collapse of their governments, by means of short-term maneuvers which will only make the crash that much worse, when it finally comes.

Argentina

Interest rates hit 40% a month on Feb. 24, responding to extreme pressure against the austral and total lack of confidence in the government's economic policies. The Argentine Industrial Union announced that it would no longer be bound by the voluntary price freeze agreement with the government, due to government's reneging on its pledge to consult with the AIU on March's price increase figures. The situation is so volatile that on March 1, a rumor of an imminent freeze of bank deposits led to a run on the banks. And then on March 2, the World Bank announced that $350 million of promised loan disbursements would be held up, pending Argentine compliance with certain terms of the loans. With no more games left to play, the Argentine government faces nearly inevitable catastrophe, no matter what it attempts.

The present crisis is the delayed consequence of the so-called Spring Plan, implemented last fall (spring in Argentina). Its main features were the brainchild of Central Bank head Luis Machinea, and were based on sweeping the general economic/financial crisis under the rug just through election day on May 14. The idea was to impose a wage-price freeze on the one hand, and to halt the devaluation of the austral with very high real interest rates, on the other. Key to the plan was building up several billion dollars worth of government reserves to be used to intervene in defense of the austral against speculators, until May, by offering interest rates so high that speculative hot money would pour into the country.

Ironically, the plan to acquire dollars worked just as it was supposed to—and yet it hasn't helped the government at

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all. Several billion dollars did flow into the country, and was promptly spent to keep the austral from collapsing. But inflation never fell below 5.7% a month (95% a year), reached in November of last year, and it has since risen to 6.8% in December (120% a year), and 8.9% in January (178% a year), with February is estimated to be over 12%, a tripling, in annual terms, since November.

The end came for the Spring Plan in February, three months earlier than the government had intended, when the demand for dollars finally became too strong and threatened to drain Central Bank reserves to zero. In the single week of Jan. 30 to Feb. 3, the Central Bank spent almost $500 million of its limited reserves to protect the austral, with no end in sight, while interest rates shot up from under 15% to 20% or more, a real rate, after adjusting for inflation, of 250% a year. To staunch the outflow of reserves, the government declared a 48-hour bank holiday Feb. 6, devalued the official exchange rate by 20%, announced it would no longer support the free market austral, and set up a third "special" exchange rate 25% higher than the official one, for imports. Interest rates were lowered to 15% a month.

Overnight, the free market rate of the austral dropped more than 75%, to 25 australs to the dollar, and then continued to fall a further 75%, as the rush out of australs into dollars continued unabated. In response, interest rates were jacked back up to 22% a month on Feb. 15, to 30% two days later, and finally to 40% a month, 28% higher than inflation (1,830% a year) on Feb. 24, which succeeded in bringing the value of the austral back to 28 to the dollar—still a very dangerous and unstable 100% devaluation from the official rate.

Meanwhile, the commercial banks have washed their hands of Argentina—as has the IMF—on the grounds that since Argentina cannot pay on its existing debt, why should the banks throw good money after bad? And on top of the disastrous financial news, both wages and the productive economy continue to rachet down. Industry, still suffering power blackouts of three hours a day, has been hit hard, while the same drought that has put much of the country's hydropower capacity out of service has devastated agriculture, now forecast to harvest only 29.8 million tons of grain, worth $3.8 billion, rather than a previously forecast 40 million tons, worth $5.5 billion.

Brazil

The situation in Brazil is similar, and only slightly less critical, to that in Argentina. Real interest rates were reported at the beginning of February to have been around 25% a month—1,350% at an annualized rate. Inflation, which had hit 70% in January, when a series of enormous price increases were put through, is said to have been cut to under 10% in February under the government's latest price freeze, but in the process, the population has suffered a devastating further loss of purchasing power, as wage increases in January were well below 70%. Despite pollyannaish statements from President José Sarney to the effect that his latest program is working, the two major union federations of Brazil, the General Confederation of Labor and the Unified Workers Central, plus a number of independent unions, have announced a general strike against the "wage losses brought on by the Summer Plan."

Driving the Brazilian crisis, like the Argentine, is the awareness that the financial edifice of the country is a house of cards. Everyone with money wants dollars, ready to flee the country at the first sign of collapse, and the demand for dollars forces the high interest rates and the erosion of currency values. Government efforts to pay debt service on the foreign debt lead to enormous internal debt—$85-90 billion in Brazil's case—which must be rolled over daily at the high interest rates.

Despite a continued record high trade surplus, the flood of dollars leaving the country has again put Brazil in the hole on its debt payments, such that President Sarney announced on Feb. 16 that Brazil doesn't have the money to pay $1.3 billion due in debt service for the month of March.

Mexico

Mexico, which presently is dedicating 59% of its entire federal budget to debt service, most of it on internal debt, has temporarily lowered inflation to the range of 20% a year, only by means of the most brutal wage slashing of any major country in Ibero-America, enforced, since early January, with a virtual police-state atmosphere against the population. Even so, inflation more than doubled in January, to 2.4%, and repressed inflationary pressures are mounting that must eventually explode. The government has kept the peso from devaluing in line with inflation, hurting manufacturing exporters, while imports are flooding the country.

Mexico has, more than any other country, gutted its productive base. Agriculture has been particularly hard hit, with the government setting prices for farmers below the costs of production, and gutting investment for irrigation. As domestic production fell, Mexico, which was nearing self-sufficiency a decade ago, imported 12 million tons, half its consumption, in 1988. Credit for the rural sector has fallen 35%.

Also during 1988, real wages of workers fell a further 17.3%, on top of more than 50% from 1982-87. GNP per capita was 16% below its 1982 level, while overall investment had fallen from 23% of GNP to 16%. Lack of investment in the Pemex oil company has stopped all exploration for natural gas, and obsolete refineries can no longer refine all the nation's gasoline.

The level of crisis is clearest in health care. Spending on health in Mexico has fallen from an already dismal 2.6% of GNP in 1982 to 1.7% in 1987, and even lower in 1988, and it is reported that almost 50% of the population has no access to regular health services, and the quality for those that do is abominable.