Brazil Challenges the International Banking System

Brazil suspends its debt payments ...and both creditors and debtors take note

In February this year, Brazil, Latin America's major debtor, declared a technical moratorium on its foreign debt. Its decision was seconded, though on a lesser scale, by Ecuador, and in declarations by Argentina, Venezuela, and other Latin American countries. The action points to the slow but sure development of a response by debtor nations to the international financial system, which, in turn, has had to make adjustments and adopt new policies to deal with this new stage of the foreign debt crisis.

Photo by Jesús Carlos.

President José Sarney.

According to official figures, Brazil's foreign debt stood at $U.S.108 billion in 1986, having risen from a 1970 figure of $5.6 billion. (A 1982 increase of $U.S. 25 billion was due to stepped-up interest rates.) Over those seventeen years, Brazil has had to pay out $U.S. 157 billion just in service fees.

Brazil does not only have the largest debt in Latin America. It also has its strongest industrial plant and export economy, and the world's third highest trade surplus (after Japan and West Germany). But it also has one of Latin America's highest poverty levels, and its economy is, moreover, only just recovering from inflation rates that had reached over 500%.

This recovery is largely due to the government economic program the Cruzado Plan, which reduced inflation 70% in 1986, stepped up economic growth, and brought about a drop in urban unemployment to 3.8% from a 1984 figure of 7.1.Despite these modest successes, however, the Cruzado Plan was never meant to deal with the enormous problem of the foreign debt; and some commentators have interpreted the moratorium as a declaration of the Plan's failure to fully reverse the Brazilian economy's negative trends.

"We cannot pay the debt if it means that our people will go hungry," stated Brazilian President José Sarney, announcing the moratorium. Thus Sarney recognized that Brazil could not continue absorbing foreign debt payments without provoking a devastating crisis in the near future. Moreover, faced with the alternative of paying the debt or encouraging economic growth, Sarney was opting for the latter —a recognition that the first alternative would imply no growth, and hence, in the long run, no possibility of paying the debt back either.

Brazil's Demands

Brazil's specific demand on its creditors is the reduction of the percentage of its Gross Domestic Product (GDP) assigned to debt servicing from 5 to 2.5%. This would mean a drop in 1987 payments from $U.S. 12 billion to six or seven billion. The difference would go to aid economic growth and also, of course, to avoid the contraction of new loans for the same amount.

In presenting the demand, Brazil offered its creditors firm guarantees: the promise to deposit payments in creditor banks, and authorize their release upon the conclusion of agreements meeting Brazil's demands. For this reason, the U.S. newspaper The *Financial Times* described Brazil's action as a "conciliatory moratorium", aimed at renegotiation rather than direct confrontation.

Photo by Jesús Carlos.

Metallurgy workers' strike in San Bernardo del Campo, San Pablo.

> **"We cannot pay the debt if it means that our people will go hungry"**

However, the Brazilian move has important implications. It represents a rejection of economic recession as a solution to the debt, and an insistence on the vital need for new loans. It is a demonstration that creditors lack a clear stand on developing a joint strategy, together with debtor nations, for resolving the problem. It has shown up international financing mechanisms as "slow and delayed", and requested their streamlining. It is an appeal to creditor nations for support and for an effective response to the needs of underdeveloped nations. Finally, it is a demand for the adoption of new solutions, on the grounds that those proposed to date have simply been ways of living with the crisis, rather than ways of overcoming it.

The repercussions of Brazil's declaration, and more generally of the Latin American debt crisis, reflect the bitter conflict affecting the entire international finance system and the U.S. foreign trade structure in particular. Since the end of last year, a debate has been raging in U.S. financial and administrative circles over proposals designed to minimize damage to that country's economic and financial structures. At least three tendencies have emerged from this debate.

One of them, adopted by the big banks led by Citicorp, would maintain the situation in force since 1982,opposing both renegotiation of the debt and the granting of new loans.

The second tendency is that advocated by the Reagan Administration — particularly by Treasury head James Baker — which seeks to maintain the current IMF-inspired program of structural adjustments, recommending new loans to debtor nations to allow minimum economic growth, with consequent punctual payment of loan interests. The third tendency is grouped round the Democrat Party's Bradley Plan, which calls for a modification of the current economic deal in favor of more flexible repayment terms, enabling Latin American economic growth to take place and with it an expansion of U.S. commerce in the region. This proposal, which basically seeks to promote U.S. trade protectionism, has been well-received by some Republicans, industrialists, and small bankers. As well, it might prove attractive to the governments and banks of Western Europe and Japan. Its only drawback is that the Democrats lack the power to implement it.

The Need for a New Formula

Thus, the Latin American foreign debt crisis has spread beyond its regional boundaries; it is on the way to becoming a destabilizing factor in the structure of U.S. trade. Its resolution necessarily involves an adjustment favoring internal economic growth in Latin American countries, which would in turn determine their future import capacity for U.S. goods. In a certain sense, Brazil's moratorium rests upon this realization, and also on the possibility of achieving a better deal from the group of creditors who lack an overall view of the problem. As well, it comes at a moment when the rest of Latin America is also beginning to take advantage of the modest opportunities available for renegotiating better repayment conditions.

With a total foreign debt estimated by CEPAL at over $US382,080 million, the nations of Latin America seem to be taking the first steps towards developing joint solutions aimed at achieving economic sovereignty. Almost at the same time as Brazil's decision, Argentina warned that it too might declare a moratorium if new loans were not forthcoming. Shortly afterwards, Venezuela stated that it would not pay its debts if the United States imposed a tax on its petroleum. In March, it was Ecuador's turn, announcing that it would not pay unless its debt was renegotiated. As for Mexico, President Miguel de la Madrid, in an interview in *The Wall Street Journal*, warned of an urgent need for a "new formula", involving further financing, for dealing with the debt.

The relationship between rich countries and poor ones must be changed

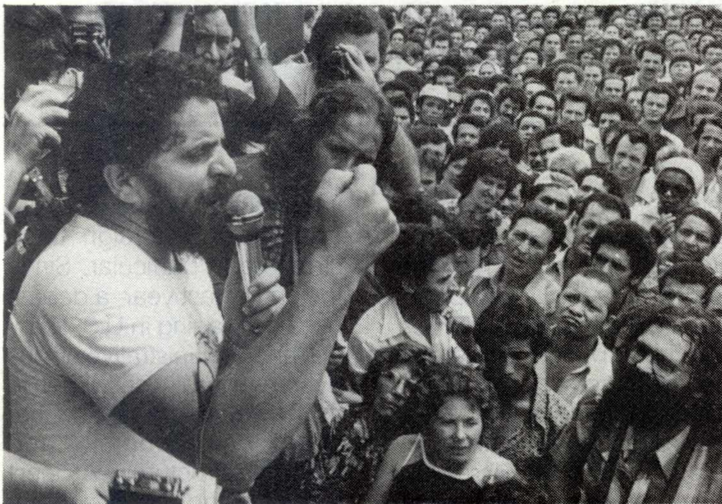

Photo by Jesus Carlos.

Luis Ignacio de Silva (Lula), Workers' Party leader.

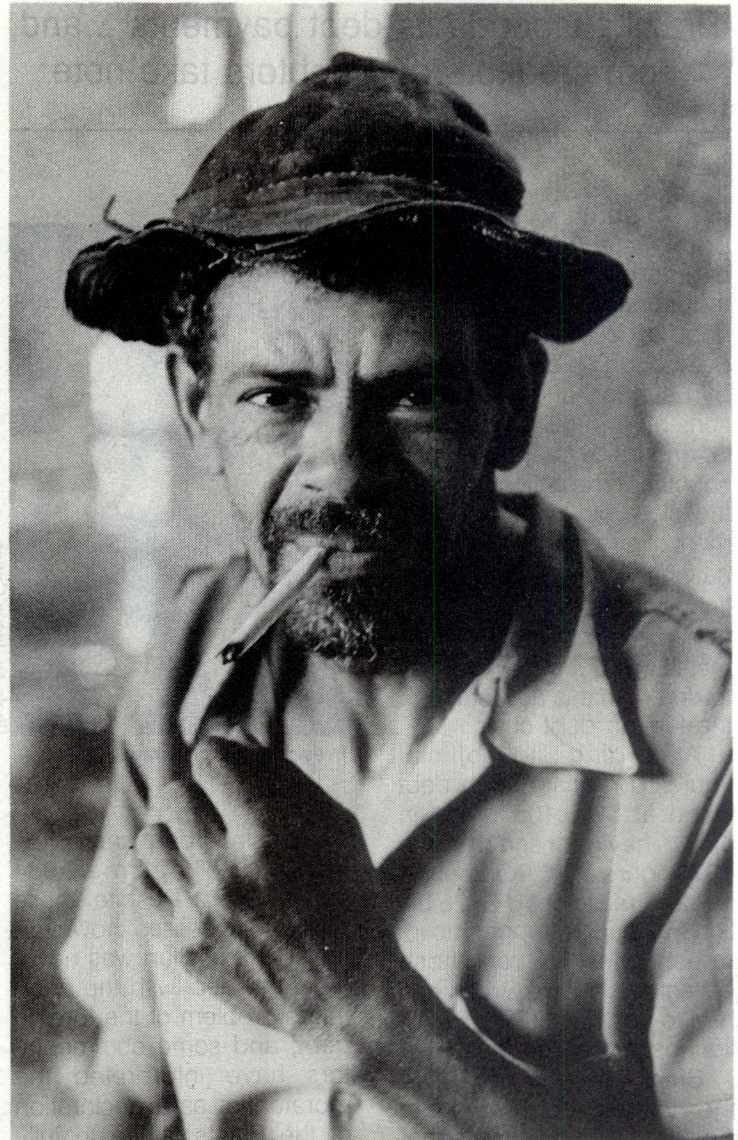

Photo by Jesus Carlos.

Peasant in Brazil's North-East.

This assertiveness, and this coincidence in actions undertaken independently , indicate the formation of a new consensus among Latin American nations which could well give rise to measures which, while perhaps not so dramatic as Brazil's, would effect substantial modifications in the relationship between creditors and debtors — which is to say, between rich countries and poor ones — in the search for a new international economic order.

In what the press has taken to calling a kind of "compulsive consciousness-raising", the international banks have had to assimilate these Latin American initiatives. Events have now escaped the control of their unilaterally-imposed structures. It is not surprising, therefore, to hear Antonio Ortiz Mena, President of the Inter-American Development Bank, and David Knox, Vice-President of the World Bank,both calling for a reversal of "the situation in which debtor countries transfer funds to the developed ones. It should be the other way round, in order to stimulate development in debtor nations."★

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