IMF and U.S. Treasury Seek Peruvian Default

"What's happening to Peru is all their own fault. They will have to suffer the consequences of a default...Let other countries see they can't get away with such things."

Frank Maresca, U.S. Treasury Department, Developing Nations Sections

The International Monetary Fund, the U.S. Treasury, and the British media are coordinating efforts to bankrupt Peru and install a fascist austerity regime there as a "lesson" to the rest of the Third World.

PERU

It is now universally recognized that Peru cannot, without substantial debt relief, pay the $942 million in debt service from it this year. The IMF is determined that Peru not get that debt relief. The American commercial banks, which as recently as late 1977 bucked IMF efforts to "pull the plug" on Peru, have now lined up behind the IMF's efforts — despite the fact that they will be the first victims of the British default scenario.

Special energy is being expended on Peru by London-linked forces because that country has served as a symbol of the Third World's drive for national development. The revolutionary process of 1968-1975 caused headaches for the domestic oligarchy, for multinationals unwilling to adapt to national planning priorities, and for bankers interested only in fast return of capital.

While Peru's present centrist military president Morales Bermudez has agreed to go three-quarters of the way with the IMF, it is that remaining one quarter that the British are now trying to extract.

IMF Accuses Peru of Violating Agreements

The IMF is trying to "pull the plug" on Morales on the grounds that "Peru has failed to meet virtually all of the targets of the stabilization programme agreed to under the stand-by arrangement," according to the *Financial Times* March 17. An IMF inspection team, headed by Linda Koenig, nosed around Lima from Feb. 14 to March 1 quietly looking for evidence of Peruvian "violations." While the IMF refuses to make any official statement on the question, its press conduits, led by London's left Fabian *Latin America Economic Report* (LAER) reported that Linda Koenig had reached the end of her tether."

The *LAER* added that the IMF has refused to disburse the meagre second $12 million payment on its stand-by arrangement, because of alleged Peruvian violations. The *Financial Times* says the IMF "found that the central bank had been cooking most of the figures" to fake international reserve levels and hide the fact that the accepted budget deficit for the year "had been overspent in the first two months of the year." *LAER* says: "the budgetary deficit must still be cut back severely, despite big savings already in health, education and public investment projects such as irrigation."

The IMF is trying to smash the "gentlemen's agreement" which has held the Peruvian sol stable at 130 soles per dollar for the last two months. It is being helped to this by the British press which smugly observes that its reports on Peru's bankruptcy will stimulate a panic to obtain foreign exchange, making rapid devaluation "certain."

There could be substantial self-fulfilling prophecy in the headline, "Peru Appears on the Verge of Default" which the *Washington Post* splashed across a page on March 14. The *Post* declared, "Peru's Central Bank will run out of money to pay the country's foreign bills by June 1 at the latest . . . Sources here (in Lima — ed.) said the most immediate internal results of default to the banks would include political upheaval beginning with a Cabinet shuffle. They predicted the possible replacement of moderate President Gen. Francisco Morales Bermúdez with a hard-line military faction that could use economic priorities as an excuse to suspend the scheduled June 4 election of a constitutional assembly."

But the *Post* story and subsequent predictions of the inevitability of a Peruvian bankruptcy in the *Financial Times* and *The Economist* were premised on a "fact" which the authors knew to be false. The press run by London financial circles claimed that the U.S. banks had cancelled a major debt refinancing package already negotiated with Peru because the IMF had disapproved of Peru's conduct. With this "big lie," the British media hoped to exacerbate Peru's economic-political crisis to precipitate the fascist coup suggested in the *Post* scenario.

The Economist fabricated a March 10 meeting of the steering committee of banks arranging the $260 million refinancing package at which the American banks (Manufacturers Hanover, Citibank, and Wells Fargo) fought against Dresdner and Bank of Tokyo efforts to procede with the loan. "After a six-hour meeting," lied *The Economist*, "the loan collapsed."

The U.S. banks, which the British media knew would also suffer from the effects of a Peruvian default, were caught with their pants down. Manufacturers Hanover

Trust, the coordinating bank of the steering committee, dashed off telegrams to the 54 other banks in the consortium urging them to keep calm, telling them that negotiations with the Peruvians were continuing, but that debt relief would only follow IMF approval.

A reliable source from one of the banks involved swore that *no* steering committee meeting took place on March 10, because "we've been postponing the meetings every week since February. Everybody's just sitting around waiting for the green light from the IMF!"

A group of experts sat in Washington last week musing about the fact that the $1.9 billion Peru owes U.S. commercial banks is larger than the entire profits made last year by the major banks. They wondered whether a declaration of Peruvian default would also undermine the capital structures of the banks. They performed a talmudic study of the Treasury Department's position (quoted above) in an effort to determine "How would bank inspectors react to a Peruvian default?" They also discussed the Third World, which they found at the Geneva UNCTAD meeting was no longer capable of putting forward a collective reaction to "case-by-case" defaults by indebted countries. They took bets on whether Turkey, Jamaica or Zambia would be the first to follow Peru into default and fascist reorganization.

Hammer "Bullish on Peru"

Just when it looked like the IMF-London operation would succeed in destabilizing President Morales, Dr. Armand Hammer, owner of Occidental Petroleum, made a dramatic intervention. The 79-year old independent oil man jumped into his private jet, flew from Los Angeles to Lima, and announced at a March 17 press conference that Oxy was going to increase its investment in Peru from the present $211 million to $500 million. Hammer explained that Occidental's new investment would enable Peru to export 100,000 barrels of crude per day by the end of this year — enough to keep Peru solvent.

Hammer maximized the political impact of his surprise visit by assuring reporters that his announcement "will greatly relieve U.S. bankers' worries over Peru's ability to repay its massive foreign debts." After meeting with top government officials, including the Navy commander widely believed to be plotting against Morales, Hammer offered Morales his much needed support: "I am willing to help President Morales Bermudez, a great leader, in any way I can for the benefit of Peru," Hammer told the press.

The problem Hammer is offering to help solve has been at the critical "blow-out" stage since the beginning of this year, if not earlier. At that point, in early February, a seven-man Peruvian government team headed by Alvaro Meneses of the Central Bank, arrived in New York to initiate refinancing negotiations. He made no bones that if their objective were not met, Peru would be obliged to default. Meneses told the bankers that Peru had $300 million in debt obligations due in February and March which could not otherwise be paid. The Treasury is penniless and Peru's trade balance is in deficit, as always during the first months of the year.

Meneses explained that Peru was "making tremendous sacrifices at a very high social cost" to insure that the 1977 trade deficit of $370 million would be turned into a surplus of $136 million this year. Despite such "dramatic progress in improving commercial balances," Peru would not be able to pay the $942 million in debt service due in 1978 without considerable refinancing, including $150 million from U.S. private banks, $100 million from their European, Japanese and Canadian counterparts, $60 million from the Soviets, and $170 million from other official lenders. Even with such postponements or new loans, Peru would run down its net international reserves (the difference between assets and liabilities due within a year) by another $150 million to reach negative $1.237 billion by the end of 1978. The Peruvians exhibited a debt profile (see Table 1) showing that debt service would eat up 48 percent of expected export revenues in both 1978 and 1979. (Economists consider 17 percent to be a danger level and 25 percent to be critical.) They pleaded with the bankers for the refinancing package to include a five-year grace period — a plea which will not be heeded.

Table 1

Peru's Foreign Debt Profile
In Millions of U.S. Dollars

	1975	1976	1977	1978	1979	1980	1981
Debt Service Payments	474	533	635	942	1.096	1.121	1.113
Amortization	284	299	390	639	764	790	773
Interest	190	234	244	285	331	331	340
New Disbursements	1.077	846	993	300	814	878	904
Total Debt (as of Dec. 31)	3.066	3.641	4.243	4.404	4.454	4.541	4.672
Debt Service/Exports Ratio (%)	37	39	36	48	48	43	37

Source: Central Reserve Bank of Peru made these estimates in Oct. 1974, based on their stabilization plan

Why the Mess in Peru? The Monetarist Myth

It has become fashionable for monetarists and even honest conservatives to attribute the disastrous financial and economic mess Peru is in to "errors" made by the Peruvian Revolution of General Juan Velasco Alvarado (1968-1975). They speak of "mismanagement," "wanton indebtedness for projects too big and too capital-intensive for Peru," "the disruptive effects of social and agrarian reforms," and "nationalizations scaring away foreign investors."

The reality is otherwise. Velasco refused to accept the backwards oligarchic Peru he took over. His social reforms, though sometimes perverted by British-inspired "local control" doctrines, were based on a humanist conception that the material and intellectual quality of the labor force is the ultimate determinant of productivity. He created a state machinery capable of planning and executing development projects on a scale beyond even the cheap rhetoric of "engineer" ex-President Belaunde Terry, who could think of little other than exporting "surplus populations"

The quality of Velasco's projects and their dollars and cents viability was recognized even by the 12-nation World Bank Consultative group for Peru ("Paris Club") in April 1975. The official news release of the World Bank stated at the time, "The group
capital requirements and agreed that to achieve the necessary disbursement levels, project loan commitments on the order of $950 million annually would be needed in the three-year period 1975-77 . . . The group discussed the list of projects prepared by the Government, amounting to $3.5 billion for 1975-1977, an amount which should enable the project loan commitments to reach the desirable level . . . . A newsworthy feature of the meeting was the lively interest expressed by group members in many of the projects included in the project list."

It is important to remember that the positive evaluation of Peru's potential by all the leading industrial capitalist countries was made on the heels of Velasco's more "radical" reforms,
companies claimed there was little oil to be found in the jungle, *after* the Peruvian fishmeal euphoria had ended, and *after* copper prices had dropped to below current levels.

"Stabilization Plan" Destroys the Economy

What is actually at the root of today's problems are the very monetarist "cures" the IMF and Morales applied to reverse Velasco's supposed mistakes. These measures have included devaluations of the sol, stringent austerity, wage cuts, import reductions, and so on. Despite whatever magical figures can be shown on Peru's account books, the national economy today has much less productive potential than when austerity began.

The labor force has been hit by huge wage cuts. The Organization of American States found in April 1977 that real wages to be *half* those of 1973, and the government admits they have been cut further since then. The result of consumption collapse from real wage reductions and strict government budgetary austerity is seen in the decline of domestic industry. Manufacturing fell by 4.7 percent through November 1977, with a rapid deceleration in the last months
Banco Continental. The hardest hit sectors were those providing consumer goods. Auto production fell by 27 percent, textiles and clothing by 15, shoes by 40, and glass by 30 percent. The only areas of significant advancement in industry were the 43 percent gain in basic metals and 5 percent in paper, as a result of new refineries and mills coming on line.

Investment levels have been decimated by the imposition of public sector austerity, the reduction of consumer demand, and drastic credit shortages. The

Peru's Balance of Payments

In Millions of U.S. Dollars

	1975	1976	1977	1978	1979	1980	1981
Exports	1,291	1,360	1,735	1,966	2,260	2,998	3,272
Imports	-2,390	-2,100	-2,095	-1,829	-1,900	-2,478	-2,840
Trade Balance	-1,099	-740	-360	137	360	520	432
Current Act. Bal.	-1,538	-1,192	-844	-337	-148	-113	-20
Total Long-Term Capital	1,135	676	665	176	102	172	249
Net International Reserve Position	116	-752	-1,089	-1,236			

Note: "Net reserves" are foreign assets minus foreign liabilities due within one year.

Source: Central Reserve Bank of Peru

World Bank estimates that 1977 gross internal investments were 17.6 percent below the level of the previous year. The decrease in reproductive investments was reflected in Finance Ministry estimates that capital goods imports were slashed in 1977 to 40 percent below the constant value level of 1975.

IMF-mandated devaluations have lowered the value of the Peruvian sol to less than a third of its 1975 value, which has naturally been reflected in rising internal inflation. In response, the Morales government has followed IMF mandates to reduce the real money supply. Banco Continental reports that real private liquidity (M1) was lowered by 7.5 percent in 1977 and the World Bank projects that the ratio of money supply to GNP in 1978 will be half of what it was in 1975. This translates into scarcity of credit, usurious interest rates, widespread bankruptcies, and the inability to finance the expansion of productive capacity.

Whatever real improvements can still be noted in Peruvian economic performance are due to capital-intensive development projects initiated during the 1968-1975 Velasco period. The only area of the economy which advanced rapidly in 1977 were copper exports, which rose by 90 percent in volume above the previous year due to the completion of the mammoth Cuajone and Cerro Verde open pits. This expansion boosted copper revenues from $227 million to almost $400 million. The added copper revenues provided half the increase in total export income. The other half came from a doubling of coffee prices and from the diversion of an additional $100 million of processed food fish and manufactures from local consumption to export markets.

Somber Prospects for 1978

The economic plan of the Morales government offers no prospects of recovery in 1978. Even if Morales survives the British default scenario and obtains a roll-over on unpayable debts, he will still lead Peru down the path of economic destruction. The only difference between what he offers and what the IMF demands is that Morales thinks "two years is too short a term" to destroy the whole country.

Morales' stabilization program calls for further devaluations and import reductions. Food and fuel subsidies are to be eliminated, causing prices of basic necessities to skyrocket. But the IMF is adamant that wages be prevented from rising more than 10 percent, and Morales is doing his best to comply. Further cuts in money supply and a 38 percent increase in tax collections which the government is pledged to achieve will place an intolerable burden on the depressed private sector.

Morales is thus continuing his eternal "balancing act," while the rats of London are nibbling away at his tightrope. As *The Financial Times* gloats: "Clearly the whole affair casts a big cloud over the standing of President Morales Bermudez . . . Bankers think he will have to put into effect an even fiercer austerity programme." *Agence France Press* reports daily rumors that the hardliners in the military are preparing to replace Morales with a repressive regime "to give the credibility the country needs to obtain an understanding with its creditors." Ex-President Fernando Belaunde Terry is openly associating himself with plotters in the Navy and factions of the Army for a coup in the name of "immediate elections." Belaunde could well serve as an Uruguayan-style civilian figurehead president for a defacto military government.

Peru Economico, a virtual campaign document published by the eager Belaunde crown, demands the following program: impose "an economic-political agreement" to pay the debt; smash wages; slash the budget; and permit foreign speculators to reposess Peru's state-owned mineral wealth. "If the political-economic agreement which must be imposed fails," they intone "then the Government will find itself obliged to use violence, its ultimate recourse."

—Mark Sonnenblick

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EXECUTIVE INTELLIGENCE REVIEW SPECIAL REPORT
DAILY ENERGY INTELLIGENCE BULLETIN
THURSDAY, JANUARY 11, 1978

LEADING U.S. BUSINESS DAILY CALLS FOR CUTOFF OF NUCLEAR COOPERATION WITH INDIA

JAN. 11 - THE WALL STREET JOURNAL, A LEADING U.S. BUSINESS DAILY RAN A MAJOR EDITORIAL TODAY CALLING ON THE CARTER ADMINISTRATION TO CUTOFF NUCLEAR COOPERATION RELATIONS WITH INDIA. IN A SCATHING DENUNCIATION OF THE CARTER VISIT TO INDIA, THE 'OPEN MIKE' INCIDENT, AND ABOVE ALL HIS COSMETIC CONCESSION THAT HE WOULD AUTHORIZE SUPPLY OF ONE SHIPMENT OF ENRICHED URANIUM TO INDIA, THE JOURNAL STATES: 'SO WHILE THERE ARE AT LEAST SOME ARGUMENTS FOR FUELING TARAPUR, THOUGH WE THINK THERE ARE BETTER ARGUMENTS FOR ENDING NUCLEAR COOPERATION COLDLY AND BLUNTLY AS THE CANADIANS DID AFTER THE INDIAN EXPLOSION. THE JOURNAL CONCLUDES, 'IT IS EASY ENOUGH TO BELIEVE THAT MR. CARTER DOESN'T NOTICE MIKES AND IS IN ADDITION SO CONFUSED HE THINKS A LETTER WILL KEEP HIS POLICY INTACT DESPITE THE HEAVY WATER SHIPMENT. BUT ON THE OTHER HAND, PERHAPS IT WAS NOT THE INDIANS WHO WERE INTENDED TO OVERHEAR THE OPEN MIKE. PERHAPS THE CANDIDATE CARTER WHO PROMISED NEVER TO TELL US A LIE WAS USING THE PLOY TO MISLEAD THE AMERICAN PEOPLE.'

WHAT IS REALLY GOING ON?

WHILE THE DUST HAS NOT YET SETTLED ON THE CARTER TRIP, BRITISH PRIME MINISTER JAMES CALLAGHAN HAS ARRIVED IN INDIA TO SUPPOSEDLY EVOLVE THE COMPROMISE FORMULA TO BRING INDIA INTO AN ACCEPTABLE STATUS ON THE NON-PROLIFERATION QUESTION. WHILE THE U.S. STATE DEPARTMENT TODAY ADAMANTLY DENIED ANY TRUTH TO THE STORY THAT CALLAGHAN 'HAS SUCCEEDED WHERE CARTER HAS FAILED,' AS PRESENTED BY THE LONDON TIMES, THE CALLAGHAN TRIP HAS OSTENSIBLY TWO GOALS. ONE, IS TO ARRIVE AT A COMPROMISE AGREEMENT WITHOUT TOTALLY DIS-CLOSING DETAILS AT THIS TIME. TODAY'S LONDON DAILY TELEGRAPH ADDS THAT CALLAGHAN HOPES TO TAKE DESAI'S SECRET 'PROMISES AND PLEDGES' TO PAKISTAN WHERE HE WOULD USE THESE ASSURANCES TO PRESS THAT COUNTRY TO AGREE TO NEW RESTRICTIONS AND SAFEGUARDS ON ITS CONTRACTED FRENCH NUCLEAR REPROCESSING PLANT. CALLAGHAN ARRIVED IN PAKISTAN JAN. 11, ONE DAY AFTER THE NEW YORK TIMES ANNOUNCED THAT FRANCE HAS REQUESTED THE PAKISTANIS CONSIDER ALTERATIONS IN CURRENT CONTRACTS.

MIDWEST COLD FREEZES OHIO COAL STOCKPILES

JAN. 11 - AS THE NATIONAL STRIKE OF U.S. COAL MINER
FIFTH WEEK, A SEVERE MIDWEST COLD FRONT HAS FROZEN
AND COAL-HANDLING MACHINERY. A SPOKESMAN FOR THE
ELECTRIC UTILITY TOLD THIS NEWS SERVICE THAT IN
CUSTOMERS HAVE BEEN ASKED TO VOLUNTARILY CUT B
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FACILITY IN SHIPPINGPORT, PA. HAS BEEN SHUT
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A DAY. HOWEVER A SECOND COLD FREEZE IS PRE
WEEKEND. THE ONGOING MINEWORKERS' STRIKE
ALTERNATIVE USED LAST WINTER DURING SEVE
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THE OHIO STATE ENERGY OFFICE DURING TH
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