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Leading LDC borrowers now face credit squeeze

by Kathy Burdman

As the financial world focused on the possibility of default by Argentina on its $34 billion foreign debt, something more sweeping may have been afoot. A close look not only at Argentina's recent financial history, but also at the total lending to all of Asia, Africa, and Latin America, reveals that a credit squeeze is under way against the entire underdeveloped sector, of a magnitude that will destroy their economies if it continues.

A study by the *EIR* economics staff shows that between 1980 and the first three months of 1982, overall bank lending to the developing sector has been reduced to zero growth, and is projected to actually decline in 1982 for the first time in decades. Total bank loans, including short-term credits and IMF loans, to the LDCs rose from 1980 to 1981 (see table below), but most of the rise was in the first half of the year, according to economists at Morgan Guaranty and the IMF, and the increase is not adjusted for inflation. The pace of lending dropped in the fourth quarter of 1981, they said, and could actually fall by as much as $9 billion in 1982, to the $60 billion range.

Coordinated cuts

The Swiss-based Bank for International Settlements (BIS) is the author of this policy, an economist at Chemical Bank revealed to a reporter April 9. Beginning in 1980, he said, the U.S. Federal Reserve, the Bank of England, the Swiss National Bank, and the other central bankers who make up the BIS, began to use their monthly Basel meetings to "establish categories" for each of their private banks' lending to major borrowers, such as Brazil, Mexico, and other countries including Argentina. Led by the Federal Reserve, the central banks then forced their commercial banks to "cut the growth" in lending.

"The key target was to reduce the net external borrowing requirement," the Chemical banker stated. Brazil, for example, was told that "unless they slowed down their borrowing, they would get no money at all," at some point, he stated.

The fall in lending to the LDCs is even more dramatic measured against the overall rise in world credit (see table) since 1980. Lending was brisk in 1981 particularly because of $42 billion in loans made to the United States for takeovers of corporations, a completely speculative activity.

Furthering this quiet LDC credit strangle may in fact be one of the major aims of the BIS and its deputies at the Bank of England in their present attempts to freeze all credit to Argentina (see article page 40). The Bank of England, which froze all loans to Argentina April 13 and is causing panicky non-British banks to

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pull back, hopes to "starve Argentina of loans but not seek to bankrupt it," the London *Sunday Times* revealed April 11.

In progress

The current credit squeeze against Argentina is an escalation of something in progress for at least a year. During 1981, Argentina's rate of world borrowing was cut to zero growth, and Argentina slashed its imports from $10.5 billion in 1980 to $9.2 billion in 1981. Consumer durables were made prohibitively expensive at home through soaring interest rates, which reduced imports of inputs, helping bring the trade deficit to a negligible $20 million, a $2.5 billion cut between 1980 and 1981 in foreign borrowing needs.

Under this austerity program, Argentina's domestic economy collapsed, with manufacturing production falling by 16 percent, subsuming a 29.3 percent collapse in auto output and a 21.4 percent collapse in textile output. Now Argentina is threatened not with zero borrowing growth, but with foreign credit cuts. "When they are forced to really cut into imports, the Argentine economy can only get worse from here on," one banker noted.

The entire underdeveloped sector, however, especially the big borrowers, is now being put through this treatment, the IMF's chief Brazilian economist, Anna-Marie Jul, stressed in an interview April 9. "Brazil is the model country," she said. "Of all potential borrowers, Brazil is more optimal to lend to than most," she noted, adding countries should "move in this direction."

Brazil had run up the world's largest foreign debt (now close to $70 billion) largely to finance its state-promoted industrialization program. In late 1980 when Brazil announced it wanted over $14 billion in 1981 to keep growing, the BIS central banks got together and laid down the law.

"Based on country risk analysis, and discussions we had with the Federal Reserve system," U.S. bankers began to turn the Brazilians down, the Chemical Bank economist explained. "They [the Fed] came around, and said, 'You should establish different categories, and no one country should represent more than a certain percentage of your capital base.' It very quickly became a big problem with Brazil. In fact, I used to tell people we should cut Brazil in half, so the percentage of the loans of each half would be less," the banker quipped.

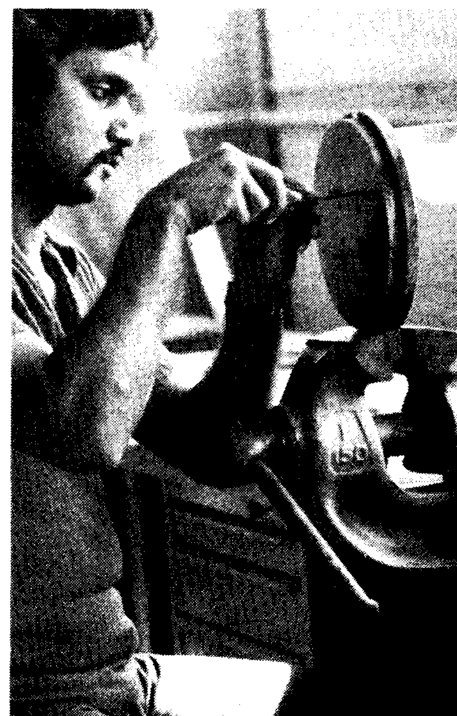
"The Fed set up prudential rules . . . as to our exposure in each particular country, and put a limit" on it, he said. Following this, Brazilian Finance Minister Delfim Netto got the same reception in London, Frankfurt, and Tokyo.

International lending, 1980-82

	1980	1981	1982 est*
To: U.S. only			
Bank loans & bonds (1 yr or more)	$ 11.1	$ 61.6**	$ 25.0
To: Europe, Japan, Canada			
Bank loans & bonds (1 yr or more)	70.0	77.4	88.8
To: underdeveloped sector			
Bank loans & bonds (1 yr or more)	24.0	33.4	30.0
IMF loans	6.4	6.2	5.5
Total	**30.4**	**39.6**	**35.5**
To: underdeveloped sector			
Short-term credits (New, less than 1 yr)	20.0	30.0	25.0
Total underdeveloped private sector	**$ 50.4**	**$ 69.6**	**$ 60.5**
TOTAL PRIVATE WORLD LENDING	**$131.5**	**$208.6**	**$174.3**
Underdeveloped sector as percent of world lending	**38%**	**33.4%**	**34.0%**

*Estimated based on figures for Jan-March, 1982
**Of which, $42 bn alone for corporate takeovers in the U.S.

SOURCE: Morgan Guaranty Bank, Chemical Bank, U.S. Treasury



The threat was so great that Brazil was forced to administratively slash imports, from $23 billion in 1980 to almost $22 billion in 1981. Meanwhile, the government raised real interest rates to the 40-50 percent level—150 percent compared to 100 percent inflation—to crush domestic demand for goods. Exports, heavily subsidized, jumped from $20.1 billion in 1980 to $23.5 billion in 1981. Brazil's trade swung from a $3 billion deficit in 1980, to a $1 billion surplus in 1981—a $4 billion reduction in Brazil's foreign borrowing requirements.

Import-cut pressure intensifies

This year, Brazil is being asked to repeat this contraction, in order to reach a net reduction in its 1982 borrowing requirement. Brazil has been asked to get its bank borrowing down from $15 billion in 1981, back to the $12 billion level of 1980. All the while, Brazil is paying out $17 billion per year in debt principal and interest to the banks.

"Brazil still has problems with its debt servicing," Jul said, "and they must manage a trade surplus of $3 billion." The IMF economist stressed that if Brazilian exports do not rise this year, as is highly unlikely given the current collapse of world trade, Brazil will simply have to cut its imports more.

The result has already been a drop in Brazil's manufacturing production by 10.2 percent in 1981, a drop which will continue this year if imports are cut. The capital-goods industry announced in mid-April that machinery production declined by 17.7 percent during 1981 because of lack of credit for new investments. In January 1982, truck production fell 71.2 percent, tractor production 61.5 percent, and crude steel 17.8 percent, compared to January 1981.

Brazil's industrialization will be crippled by the import cuts. "Projects will not be able to import any new machinery," Jul stated. "And there will be no new projects begun." Eleven major hydroelectric dam projects and 6 out of 8 nuclear power plants on order have been postponed.

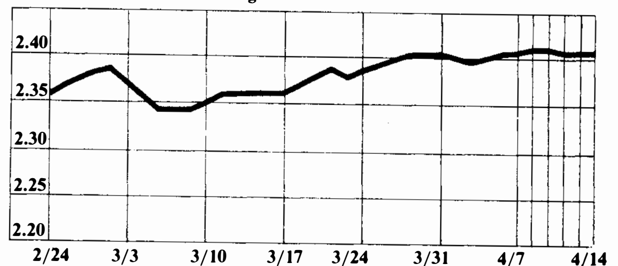
A parallel situation is occuring in Mexico after the recent devaluation, IMF officials told reporters recently. As *EIR* has reported, the Federal Reserve has told the banks to "put some pressure on Mexico to reduce their borrowing needs," as Fed officials put it, and bankers say although Mexico needs at least $20 billion this year to get by, it will be lucky to get $14-$15 billion, meaning zero growth in external financing from 1981.

To cut borrowing, the IMF and international bankers are advising Mexico to cut its imports by as much as $8 billion this year, that is, by almost 25 percent from 1981. Mexican imports for January and February were in fact down by 20 percent compared to 1981.

Currency Rates

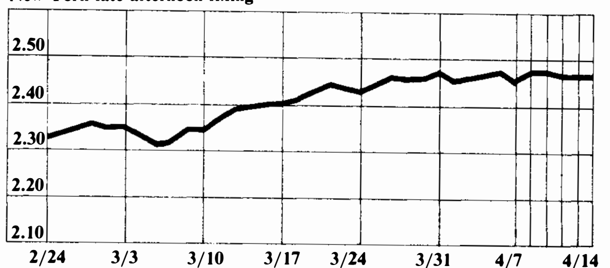
The dollar in deutschemarks

New York late afternoon fixing



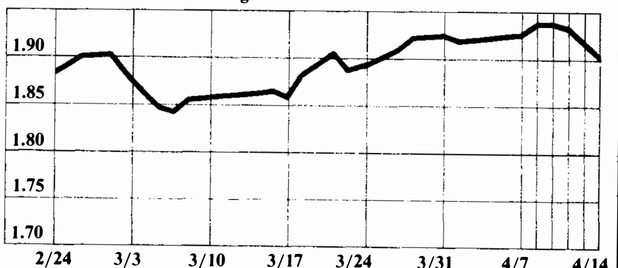
The dollar in yen

New York late afternoon fixing



The dollar in Swiss francs

New York late afternoon fixing



The British pound in dollars

New York late afternoon fixing