How Morgan rigged Brazil's debt crisis

by Mark Sonnenblick

The world financial system has been hanging by a thread for the past two weeks over the fate of Brazil's efforts to renegotiate $27.2 billion of its foreign debt.

As all players in the game know, a Brazilian default on its $90 billion debt could break the back of the international banking system. *EIR* has uncovered one of the most bizarre stories of modern financial history in the way British-run Morgan Guaranty Bank took control over, and proceeded to wreck from the inside, the Brazilian debt renegotiation. Everything indicates that Morgan is trying to bring down the whole house of cards.

On Dec. 20th, the three top Brazilian financial officials gathered 125 of their largest creditors at New York's Plaza Hotel. *EIR* and some of the more diligent bank economists expected Brazil to announce a moratorium and full-scale restructuring of its debts. Instead, Brazil presented a complex four-point program for rolling over all forms of long- and short-term loans from the banks and getting $4.4 billion in new loans to help meet interest payments. There was general agreement among bankers the next day that they would accept the four-point package.

When the bankers arrived in their offices Dec. 30, the day on which they were to telex their responses to the Brazilian program, they found a telex signed by the Brazilian Central Bank announcing that Brazil would withhold repayment of principal on long- and medium-term debt starting January 3; they also found a Reuters wire misreporting that Brazil had declared a unilateral debt moratorium and that Finance Minister Ernane Galveas had resigned in protest.

On Dec. 31 Morgan Guaranty, the bank controlling the debt renegotiations, reported that commitments had been received thus far, for only $1 billion of the $4.4 billion in new loans. Hopes for a trauma-free debt rollover evaporated.

Brazil submits to banker receivership

'Why was the Brazil debt renegotiation so badly botched?' bankers are asking each other. Certainly it is not through any failure of Brazil's economic austerity program. Brazil's entire 1983 economic policy had been calculated backwards from Morgan's assessment that bankers would be willing to provide Brazil with a maximum of $5.9 billion in new exposure, Planning Minister Delfim Netto told the press (see *EIR* Nov. 30). And when Morgan lowered that figure to $4.4 billion, Brazil took another slice out of public sector import and investment budgets. Brazil signed a tentative agreement with the International Monetary Fund (IMF) in "record time" because Morgan Vice Presidents Tony Gebauer and Gerard Finneran and retired Citibank Vice President "Al" Costanzo had already done everything but cross the t's and dot the i's on Brazil's letter of intent. In effect, Brazil was placing its internal economic policy under the receivership of those three veteran bankers.

The Brazilians put up a dazzling performance for the bankers at the Plaza Hotel event Dec. 20—with a comprehensive compendium of debt statistics and a demonstration of how Brazil would avoid a default. And—for the clincher—Jacques de Larosiére, the head of the IMF, put his institution's reputation on the line in support of Brazil's "viable, coherent, and consistent" program. Bob Lorenz of Security Pacific commented, "de Larosiére came in with a machine gun and put it on the table."

The entire IMF-backed program, however, is based on a fraudulent premise—that Brazil will achieve a $6 billion trade surplus in 1983. Last year, Brazil eked out an $800 million surplus at the price of keeping the country deep in the recession which began in 1981 and of burning up stockpiles of oil and other imported materials. Today Brazil exports almost twice the volume of its products per unit of imports as it did in 1979. One by one, its newly won Ibero-American and Asian markets have been knocked out by the banks and the IMF. Brazil's exports to the Latin American region were down by 31 percent during the first 10 months of 1982.

EIR asked Brazilian Planning Minister Delfim Netto what Brazil would do if the world economy and world trade conditions continued to deteriorate. Brazil's economic mastermind replied, "If you say there will be a 10 percent decline in world trade in 1983, then not only will Brazil collapse, but the whole world will collapse."

'Morgan shoved it down our throats'

When representatives of the top 20 banks returned to the Plaza Dec. 21 to negotiate implementation of the four-point program, the euphoria rapidly faded, despite the blandishments of the Morgan-Citibank crew. François Brunt of Banque Nacional de Paris stormed out of the meeting protesting the way everything had been "predetermined unfairly" by the Morgan group. "What shot the whole thing up from the beginning," a Brazil analyst at one of the largest Wall Street banks later complained, "is the way Morgan and Citibank shoved the thing down our throats, with no consultation with the other banks or anything and no time to decide. There was lots of resentment that they had known everything for months and had kept all the rest in the dark."

The telex sent at the end of the Dec. 21 meeting to Brazil's 1,114 creditor banks over the signature of central bank president C. G. Langoni concluded, "We ask that on about Dec.

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What Brazil demands of its international creditors

Brazilian central bank president C. G. Langoni presented bankers with four proposals Dec. 20. He insisted *all four* had to be accepted by Dec. 31—later extended to March 1. Langoni left it to Citibank and his aide, C. M. Serrano, to threaten debt moratoria if the bankers delayed.

Project 1—*New Money Facility*

Calls for: $4.4 billion in new loans to Brazil.

Status: Regarded by bankers as the "simplest component." Morgan leaked that "over $1 billion" had been committed by Dec. 31. Langoni claimed $2.5 billion committed by Jan. 4. European and most small banks balking on increasing exposures.

Project 2—*1983 Debt Amortization*

Calls for: All $4 billion in principal due to be repaid to banks to be re-loaned to Brazilian entities for eight years with 30 months grace.

Status: December 29 telex announced Central Bank would *de facto* withhold all amortization payments to creditors starting Jan. 3 to force banks to keep money in Brazil. Interest payments would continue. Any bank could possibly declare Brazil "in default," and turn entire $90 billion Brazilian debt into default. Most banks were planning to roll over these debts anyway. Involuntary nature of retention is only problem. Bank consent, making this legal, expected Jan. 7.

Project 3—*Short-term Debt*

Calls for: banks to continue revolving credits for Brazil's raw material imports and for prefinancing Brazilian exports at current $8.8 billion level.

Status: Theoretically should be no problem. But Brazilian Exporters' Association warns banks have been refusing export prefinancing, thereby truncating Brazil's capacity to export.

Project 4—*Money Market Lines*

Calls for: All banks to restore short-term bank-to-bank exposure to Brazilian banks to June 30, 1982 level of $10 billion.

Status: Few banks will voluntarily accept this; they have been closing down these lines since August, wiping out first the liquidity of Brazilian banks and then the nation's reserves. Few lenders are willing to put funds into insolvent offshore Brazilian branch banks which could be (and should have been) hived off as Ambrosiano Holding (Luxembourg) was by Italy.

30, 1982, the gentlemen send us a telex accepting our proposals to Morgan Guaranty Trust Co. of New York." As if it were running a classic operation of vote fraud, Morgan wanted to count the "returns" in its own inner sanctum.

The confusingly written telex which announced Brazil's partial moratorium Dec. 29 was apparently also a Morgan invention. Brazil's top business daily, *Gazeta Mercantil*, reported "central bank foreign area director Carlos Madeira Serrano said the telex sent abroad was drafted by the big banks and only signed by the central bank." By Jan. 4, a senior adviser in the Reagan administration confided to *EIR* his assessment that "the Brazil loan has fallen through."'

Brazil lost 95 percent of its export revenues to debt service during 1982, not counting the billions of dollars lost by evaporation of short-term credit lines. It paid $7.8 billion in amortization and almost $11.5 billion in interest, according to central bank estimates. It managed to avoid a formal default only by scraping up $2.4 billion in "bridge-loans" from the U.S. Treasury, the BIS, and a half-dozen of the largest American banks.

The Brazilian "bailout" was politically managed by George Shultz in order to prevent Brazil from joining with other similarly penniless Ibero-American nations to force a renegotiation of the debt along the lines proposed by economist Lyndon LaRouche, on a program which would permit rapidly growing inflows of high-technology capital goods from the North. Instead, Shultz suckered the Brazilian military leadership to go the IMF route with promises of "U.S. government support," a U.S. recovery, and a "practically automatic" approval from the IMF and the banks.

An end to growth?

There was manic rejoicing over Brazil's misfortune at the *New York Times*. It celebrated Dec. 18: "With its agreement on terms for an IMF loan, Brazil appears to have temporarily applied the brakes to its rush toward the status of a great industrial power." The *Times* intoned that the banker dictatorship "means that the Government will not have the wherewithal to continue its huge investments in industrial projects, especially steel and hydroelectric power." But, while the economic ministers were putting on a fine show for the bankers, Nuclebras contracted civil construction for two more nuclear power stations in Sao Paulo. In a country now letting 25 percent of its electric capacity go unused, further nuclear starts are a dramatic assertion that Brazilian growth will soon require even more energy.

Stanford University's Latin American Studies director, Dr. John Wirth, recently offered an expert assessment shared by many of the bankers who understand the impact of Brazil's rapid development: "The self-confidence of the Brazilian military is extraordinary. If they see the world economy is not able to provide trade opportunities and finances, . . . there is a great danger they will declare a moratorium. They will do it and they have the will to do it if they feel they are being worked over."