Behind the debt stretch-out: Volcker's colonial economics

by Kathy Burdman

Since Mexico announced bankruptcy in August 1982, the world has been told that an international "debt crisis" has arisen because of Ibero-American nations' profligate borrowing and spending. Recently, central bankers have reported that the debt crisis is now "under control," as Swiss-based Bank for International Settlements (BIS) president Fritz Leutwiler told the Swiss Institute for Foreign Research on Nov. 16.

But the current crisis is not a "debt crisis"; it was not caused by Mexico, Brazil, or any other Ibero-American nation; and it is far from over.

There exists a world *banking* crisis, which was deliberately created by central bankers and commercial banks, in order to introduce a "new Bretton Woods" monetary system.

This reorganization, already well under way, would take the sovereign control over credit away from nation-states, and place them under a dictatorship of central banks and private banks.

Anatomy of a conspiracy

It is absolutely true that Mexico, Brazil, and the rest of Ibero-America are now bankrupt, with vast, unpayable debts. From 1980 to the present, Mexico's debt has leaped from $60 billion to $90 billion, Brazil's from $60 billion to $95 billion, and that of Ibero-America as a whole from $200 billion to $350 billion. Since the beginning of 1983, Mexico has been the only large debtor on the continent able even to make interest payments upon this debt.

But the debtors did not create this situation.

The fact is that beginning in the fall of 1981, a decision was made by the Swiss-based BIS, the International Monetary Fund (IMF), and the British Commonwealth Secretariat to reorganize the world banking system. First, a series of policy statements was made calling for the reorganizaton:

- In August, 1981, British Commonwealth Secretary Sridath Ramphal called for the formation of a "new Bretton Woods" monetary system, with a "new world central bank" to control world credit allocation.

The British Empire set up a 19th century creditors' cartel to force Egypt to pay its debts, as bankers are doing in Ibero-America today. When the British plan failed, the Royal Navy moved in. Shown here are the ruins of Alexandria after naval bombardment in 1881.

- In September 1981, the quondam BIS president, Jelle Zijlstra, speaking at the 1981 IMF annual meeting, called for a "new Bretton Woods" currency system to give the BIS central banks "surveillance" control over nations.
- In March 1982, BIS president Fritz Leutwiler in a Mainz speech called for the formation of a creditors' cartel, an "ad hoc body" to "tighten lending."
- In June 1982, Britain's Lord Harold Lever called for the creation of a "new international bank" which would "put a stop to too much international lending."

No sooner was the reorganization proposed than a formal creditors' cartel was set up to conduct the bankruptcy proceedings on the existing system. On May 13-15, 1982 the *Ditchley Group* was formed at Ditchley Park in London. Members included over 36 international commercial banks, along with the senior officials of the BIS, IMF, Bank of England, and U.S. Federal Reserve. BIS managing director Alexandre Lamfalussy and IMF managing director Jacques de Larosière attended the founding meeting.

No sooner was the cartel formed than nations of Ibero-America were deliberately bankrupted, as a matter of policy. They did not go bankrupt; in fact, Argentina and Mexico "were perfectly viable debtors," as one IMF official put it at the time. "But the banks have made a decision," he said, "to cut off credit against every nation, *bankrupt or viable,* until they come to the IMF" and submit to the Fund's conditionalities.

For no commercial reason whatsoever, lending to Ibero-America, which had been rising at $8 billion a quarter up to the second quarter of 1982, collapsed to $2.7 billion in the third quarter, right after Ditchley was founded. Lending to the Third World in general, which had been rising at a rate of $13 billion in the second quarter of 1982, came to a sharp halt and fell to $3.8 billion in the third quarter.

Britain's April 1982 shooting war against Argentina over the Malvinas was used as an excuse; it was said Ibero-America was termed a "political risk." The fact is that the creditors pulled the plug.

The premeditated credit cutoff in turn generated another series of measures which forced the debtors further into bankruptcy. During the Malvinas war, as credits were cut to Mexico, for example, speculation was mounted against the Mexican peso, triggering an exponential rise in Mexican capital flight and the collapse of the peso in June. The Argentine peso received the same treatment. In Brazil, capital flight was so intense that reserves collapsed during the third quarter of 1982. (See **Figures 1** and **2.**)

As foreign credits were cut and currencies' purchasing power abroad collapsed, Ibero-American trade went into the barrel. Mexico, which needs imports to industrialize, went from a trade deficit into a massive trade surplus during the third quarter of 1982, as the IMF insisted that its imports be cut by $8 billion during 1982. Instead of importing capital, Mexico shipped not only oil but capital abroad. By August, 1982, Mexico was formally bankrupt.

New Bretton Woods: old British imperialism

Once the "debt crisis" was forced upon the debtors in the third quarter of 1982, the fourth quarter saw over a dozen proposals for restructuring of world banking. All these schemes were presented as "debt relief" for the Third World, in which the creditors offered a debt "stretch-out"—a reduction in annual payments of principal and interest, to help out the debtor and overcome the crisis.

The catch was that each plan would establish a 19th-century style British imperial system of looting of the debtor's economy. In return for the stretch-out, the debtor had to turn over "equity" or other rights to garner revenue from its national income—surrendering national sovereignty to a private banking cartel.

The plans were of two types. Some proposed a medium-term stretch-out of the portions of debt coming due this year, which obviously could not be paid. Bank of Italy director Giovanni Magnifico proposed in December 1982 that "a portion of the short-term debt" be stretched out by the World Bank over 10 to 12 years. U.S. National Security Council official Norman Bailey proposed in March 1983 that current annual debt payments, 18-20 percent of total debt, be stretched over three to eight years.

Plans such as Bailey's to reduce the annual debt payments to a "prudent level," call for an "Exchange Participation Note" (EPN) to be directly issued by the central banks of debtor nations to private bank creditors in exchange for existing unpayable debt IOUs. The payments on EPNs would be "stretched" relative to the old debt payment schedules.

In return, however, the banks would be given "equity" ownership of the national income of the debtor nation. The EPN would be paid by sequestering revenue, upon which EPN-holding creditors would have first lien, from the export and other foreign earnings of the debtor. The creditors would form "collection committees" for each debtor country and take over its finances completely.

A more extensive set of plans was proposed in December 1982 by British Commonwealth spokesmen such as former British Labour Party cabinet official Lord Harold Lever, in February 1983 by his protégé Felix Rohatyn of Lazard Frères, and in April 1983 by Greek central bank governor Minos Zoambanakis. They called for the entire $300 billion in short-term debt payments due from the Third World, or about 40 percent of the entire Third World debt of $700 billion over the next year, to be "stretched out." Zoambanakis wanted to keep the stretch-out at medium term, over 13 to 25 years; Lever and Rohatyn proposed to extend it over 25 to 30 years.

This second group of proposals envisioned a "new international institution" to buy out large amounts of the debt and centralize the stretch-out over a full 30 years. Such a "New Bretton Woods" agreement would give the underdeveloped countries more voting rights than the old 1944 Bretton Woods IMF-based system, promoting the the illusion that they were "democratically" participating in "equal sacrifice" for all. Debtors would supposedly accept the very policies by means of "global consensus" which they would reject were such imposed on them.

The new institution would also restructure debt through a *debt exchange*. The new institution would place its own long-term bonds with the private banks and take on their holdings of LDC short-term debt. Such a world central bank could dictate economic policy to debtors for the next 30 years, through its control over negotiations on the debt. The new bank would become the creditors' collection agency; it would attempt, not to collect all the debt, but to manage the economies of the debtors.

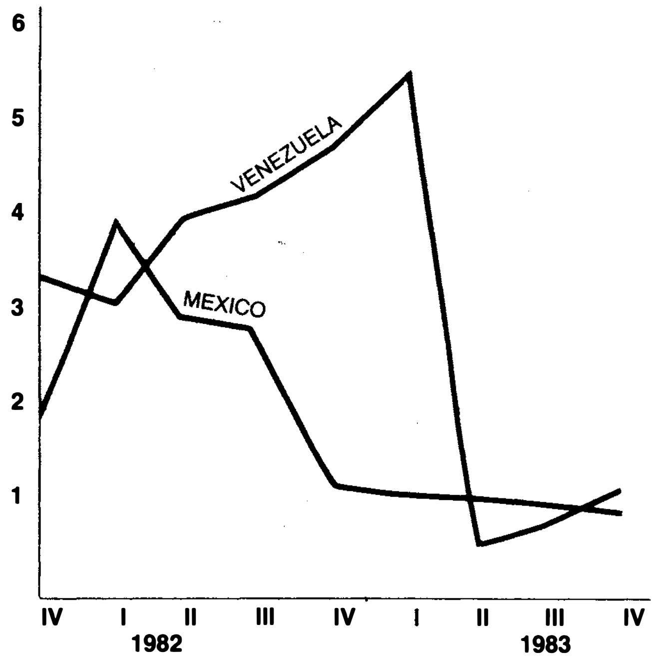
Already in effect

In fact, even as the plans were proposed, the restructuring had already begun.

What has been accomplished is the kind of looting program described for the hypothetical country of Modelia by Norman Bailey in his March 1983 article in *Georgetown Review*. Modelia, with a $40 billion foreign debt, had a 1983 debt service bill (combined principal and interest) of $7 billion. Under a tough IMF conditionality program which forced imports well below exports, Modelia was running a $10 billion trade surplus. Modelia's $7 billion 1983 bill was stretched out over three years, and the $2.3 billion annual payments were attached.

Since the creditors' cartel cut off loans to Ibero-America

Figure 1
Capital flight
billions of dollars



in the third quarter of 1982, every debtor there has undergone that sort of "stretch-out." In March 1983, for example, Mexico received a "stretch-out" of its 1982 and 1983 principal, a sum of $19.5 billion, over nine years to 1992. In February 1983 and November 1983, Brazil was granted a stretch-out of its $16.8 billion debt service for 1982 and 1983 over the same nine-year period.

In fact, every country in Ibero-America has had its 1982 and 1983 debt payments stretched out, over an average term of eight to nine years, for a total of 25 percent of the countries' combined $300 billion debt, as follows:

Mexico	$19.5 billion
Brazil	16.8
Argentina	12.0
Venezuela	18.4
Chile	4.7
Peru	1.4
Ecuador	2.8
Total:	$76 billion

And yet, the stretch-out plans having been implemented, the countries are worse off than before. Their total debt continues to climb. The more than $200 billion in debt which comes due once again in 1984 is being used, as one Brazilian diplomat put it, "to keep the water level rising to just below our noses."

Above all, the countries have begun to relinquish their national sovereignty. They have been forced, in exchange for the stretch-out, to grant the creditors' committees control over the revenues of their countries.

The 1984 plan

The next step in the plan for an imperial world banking system will be to expand the International Monetary Fund, which is run by the BIS central banks, into an actual world central bank which will directly control the economies, currencies, and debt of both debtor and creditor nations, including the United States.

Set for next year is a conference of the Group of 10 finance ministers to discuss the new Bretton Woods currency system put forward by then-BIS chief Jelle Zijlstra. Zijlstra proposed that the IMF oversee a currency system of "fixed but adjustable rates of exchange" to control the rate at which the United States and other OECD nations can create credit. He proposed to peg the dollar to gold, not to reduce inflation, but to force contraction of dollar credit.

In order to keep currencies in line, he proposed that the United States, as well as the Third World, surrender its sovereignty to the IMF, by giving it "surveillance" over nations' domestic credit, control over all budget deficits and wage and price policies.

As part of the "equity" plans already implemented to "stretch out" debt in Mexico, Argentina, and Brazil, prototype currency programs for the new Bretton Woods have already been introduced. Under a current IMF plan, parts of Brazil's foreign dollar debt are being denominated in Brazilian cruzeiros and held as "blocked accounts" owned by the creditors at the Brazilian central bank (see article, page 26). By the end of 1984, this debt could build up into 6 to 10 trillion Brazilian cruzeiros—*and the banks plan to demand that Brazil allow them to buy up Brazilian assets with the accounts*.

The IMF is planning to establish a $12 billion SDR "Interest Guarantee Fund" to guarantee these cruzeiro accounts, that is, to guarantee an IMF-mandated cruzeiro/dollar exchange rate.

Simultaneously going into place is a plan by BIS circles for internationalizing the dollar. The Brazilian cruzeiro, Argentine peso, and other currencies are becoming so devalued in the eyes of their citizens that U.S. dollars have begun to circulate as the currency of daily exchange in these countries. This inflates and devalues the dollar in global terms. Thus all currencies are being undermined and inflated by the debt payments process. This opens the way for Zijlstra's deflationary currency reorganization by the BIS central banks.

Figure 2
Reserves
billions of dollars