Poland was held hostage by the banks at the end of World War I for a measly $25 million loan to get the war-ravaged economy back on its feet. Poland had four different depreciated currencies in different zones of the country—German marks, Austro-Hungarian kronen, Russian rubles, and German-Polish marks. Norman and Strong created a new currency, the zloty. But they held up the loan *until 1927*, when the Polish government finally agreed 1) to renounce the right to issue any paper currency, entrusting that instead to the central bank, 2) to run budget surpluses, 3) to restrict part of the loan "to increase the capital of the Bank of Poland," and 4) to accept a foreign adviser on the board of the Bank of Poland. Poland complied, surrendering its sovereignty.

Romania was forced to agree to pay off tens of millions of dollars of prewar debts before Norman and Strong would allow it to tap the international credit markets.

In 1924 Norman and Strong decided to put heavily-indebted Europe under the discipline of a contractionary gold system. Britain joined the gold standard in 1925—after shutting down a section of its industry—and other European and eastern European countries were forced to join the gold standard before they could get new loans. The contractionary gold standard within a Europe bloated by escalating levels of interindebtedness was the perfect recipe for disaster, which hit fully with the 1931 Kreditanstalt collapse.

The same deflationary recipe is being demanded again today to solve Ibero-America's debt problems.

The *fondi* vs. the United States

Since 1876 the *fondi* have used the U.S. dollar as the instrument to bail out the world monetary system. Never during this time has the dollar been under the sovereign control of the U.S. government, nor has it been used, as it should be, to finance world trade and industry.

Starting with the Specie Resumption Act of 1875, the U.S. currency was placed on a gold standard and made a junior partner to the pound sterling—an arrangement which allowed the pound to attach the dollar's wealth. In 1913 the U.S. Federal Reserve was created for the express purpose of financing Britain's role in World War I.

At the Versailles peace conference, the dollar was internationalized. New York became in 1924 the chief lending market for world debt management.

After World War II the dollar was made the international debt currency, and a huge mass of claims arose against it, now totaling $1.7 trillion on the Eurodollar market—threatening the dollar with bankruptcy if the system collapses. In November of this year, the dollar once again was called upon to bail out the *fondi*: the U.S. Congress was blackmailed into allocating an $8.4 billion bail-out to one of the chief instruments of the *fondi*'s creditors' cartel, the International Monetary Fund. Now the *fondi* plan to bring down the overextended and overexposed world dollar system and the United States with the same surgical precision they used to topple the Ottoman and Austro-Hungarian Empires 100 years ago.

Banks defy sovereignty,

by Christian Curtis

"They may *think* they can take over our assets," a senior executive in a Brazilian state firm said angrily when told by *EIR* of the objectives of the bankers' cartel. "But they're crazy if they think they can get away with it."

The banks, however, are getting away with it. The scheme is being sold under the rubric of "debt relief."

Within the past 16 months, Ibero-America has been transformed from a region of immense development promise into a group of economies with the profiles of classical colonies. These nations have become record net exporters. Their revenues are funneled entirely to the world financial centers. Their currencies have been devalued by up to 2,000 percent, which has made imports practically prohibited and has turned their governments from sovereign economic powers into mere administrators for foreign interests. Simultaneously, these governments have signed away sovereignty through contracts that grant foreign banks access to state sector assets, submit their citizens to the jurisdiction of foreign courts, and allow creditors to buy up national resources at ever-cheaper prices.

At the same time, contrary to those Ibero-American leaders who think they are "getting by," the debt bill continues to grow through refinancings, and no principal is being retired. Beginning roughly in the first quarter of this year, even interest payments were falling into arrears (see **Figure 1**).

Ibero-America is ripe for colonialist looting. It will be relatively easy for the creditors to compel the Ibero-Americans to surrender equity—mineral deposits, land, tax liens, utilities, plant, and equipment—in exchange for "generous" concessions on terms and interest rates.

Almost every debtor had its late 1982-83 principal payments rescheduled—either formally or de facto through moratoria and rollovers—usually over eight or nine years. Is this relief? Quite the contrary. The patterns of trade and currency devaluations shown in the accompanying graphs explain the real cost Ibero-America is paying to have its debt "stretched out."

The crucial point is not the absolute amount of debt falling due over a given period, or even the rate of interest. Rather it is *how much of a debtor's earnings are devoted to servicing*

grab debtors' assets

the debt. The size of the debt is irrelevant.

Compare the trade patterns in **Figure 2** for 1981 and 1983. Before debt restructuring ("relief") began toward the end of 1982, Mexico, for example, ran a trade deficit. Yet the terms of its debt were supposedly worse, with some $20 billion falling due between August 1982 and August 1983. After "relief" Mexico, with its debt stretched out nicely over eight years, shows a record trade surplus of close to $14 billion.

What is wrong? Before "relief" Mexico got enough credit to cover its trade deficit, i.e., it could still import crucial capital goods for development projects. After "relief" essentially every dollar earned from the trade surplus—which is based almost exclusively on the gutting of imports—has been devoted to meeting annual interest payments, around $12 billion in 1983.

The same pattern occurs in almost every case. In 1981 the Ibero-American debtors were all either net importers or ran small export surpluses, and were borrowing heavily to finance deficits. Credit was cut off by September 1982. In 1983 every one of the four largest debtors is running record export surpluses. In every case the surplus is generated as imports collapse faster than exports. With the absence of new loans, the entire surplus, some $27 billion, fails to cover the $31.5 billion in 1983 interest charges.

But the situation is even worse than this. **Figure 3** shows what has happened to the currencies of the four largest debtors. In every case the curve indicating devaluation changes its exponential growth pattern beginning approximately in the third quarter of 1982. The creditors forced the destruction of every major Ibero-American currency almost simultaneously—either formally (by outright IMF demand) or informally (through well-timed runs against key Ibero-American currencies by the financial cartel).

This had two disastrous consequences. First, the Ibero-American debtors were forced to become huge net exporters. Imported commodities denominated in dollars became prohibitively expensive, and locally made items became dirt cheap to foreign buyers. Second, the Ibero-American gov-

Figure 1
Arrears
billions of dollars

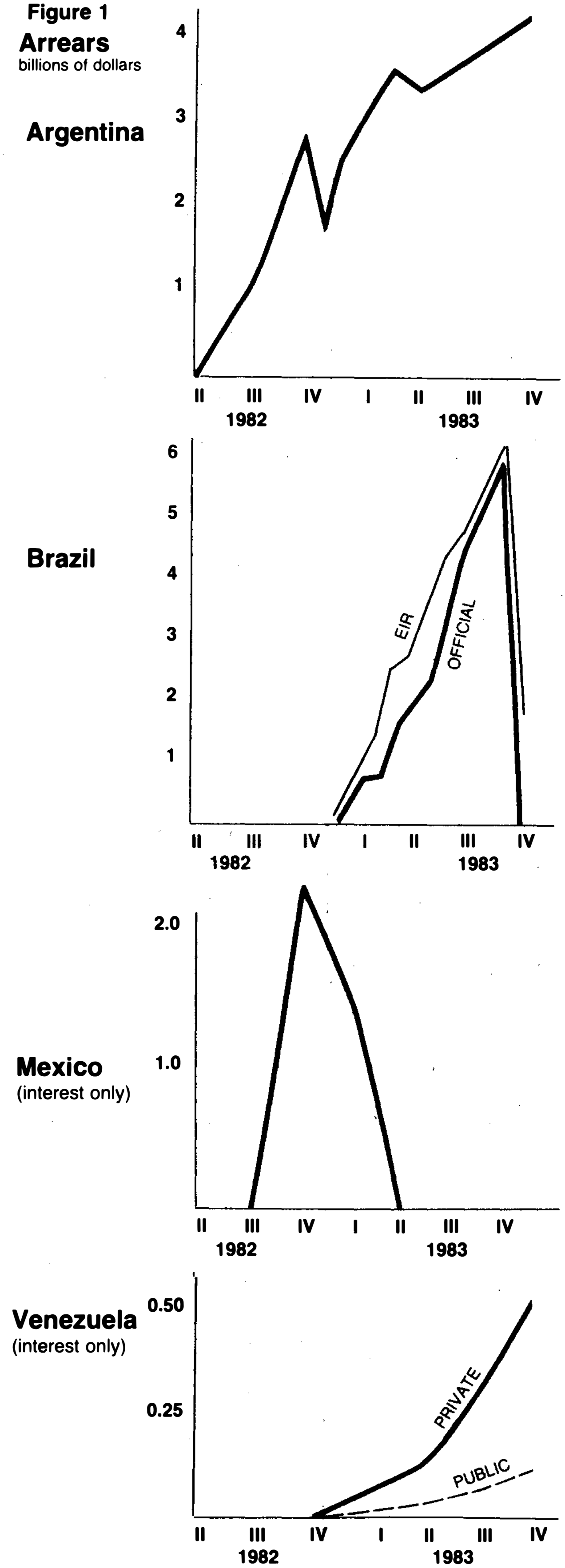
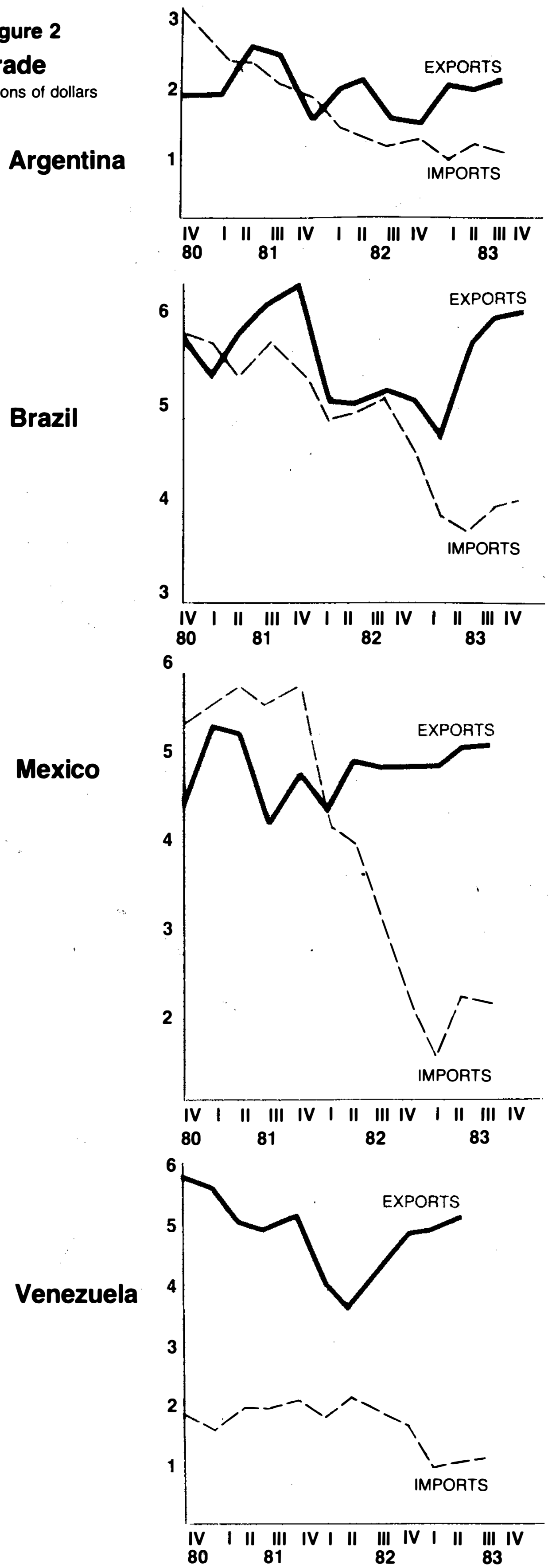


Figure 2
Trade
billions of dollars



ernments lost sovereign control over their currencies, and with it, control over their domestic credit and assets. The assets the creditors eventually want to seize are becoming cheaper by the day, and the debtors are being left increasingly unable to prevent it.

Meanwhile, notice that in **Figure 4,** new loans going into Ibero-America plunge by more than 80 percent during the last two quarters of 1982. In sum, between 1981 and 1983 Mexico's credit was cut off, its ability to import was demolished, and almost 100 percent of its revenues is now devoted to interest payments.

The 'equity' schemes

The basic idea behind all "equity" plans is simple: the debt is exchanged for some form of ownership in the debtor nation. Direct equity seizure is simplest. It does not require creation of "new institutions," nor the involvement of creditor governments. The debtor and creditor simply agree to reorganize their paper. Bank creditors would agree to exchange the short-term debt IOUs of a given Third World country for "equity" ownership of the debtor nation's *general national revenues.*

This version was proposed by U.S. National Security Council chief international economist Norman Bailey, who called for the creation of an equity instrument, the Exchange Participation Note (EPN), in January 1983 (see article, page 20). Later, at monetary conferences in Vail, Colorado and in Geneva, Switzerland, Henry Kissinger, along with his economics adviser Alan Greenspan, made parallel proposals for "equity ownership" of Third World assets.

Under a second kind of equity plan, creditors would demand that the debtor change its laws on foreign investment, and allow creditors to convert the IOUs of Third World state corporations and private corporations into *direct equity ownership of those companies* by foreign private investors.

"The laws in Latin America on foreign investment must be changed, and that is a problem of national sovereignty," said an adviser to Kissinger at the Council of the Americas.

'Blocked currency'

A more subtle variant of the direct equity seizure is the "blocked currency" plan. The scheme is being masterminded by Bank of America and Security Pacific bank, the bank of the Aspen Institute. These banks argue that half of Brazil's debt should be converted into cruzeiros, the national currency. Interest would still be paid on the cruzeiro portion of the debt, but into a blocked account at the Brazilian central bank.

There is a hitch, from the American side. Under U.S. law, interest paid in a foreign account in a foreign currency is not a legitimate performing asset. To remedy this problem, U.S. Federal Reserve Chairman Paul Volcker is calling for an IMF "interest-rate subsidy fund" to insure the blocked currency accounts. This ultimately means that the U.S. government will have to pick up the tab for the entire scheme should anything go wrong.

The banks would be amassing huge amounts of Brazilian domestic currency. By the end of 1984, foreign banks could be holding anywhere from 6 to 10 trillion cruzeiros, enough to buy up quite a bit of Brazilian assets. Furthermore, each time the cruzeiro is devalued under IMF pressure, which is very frequently, billions more cruzeiros would have to go into the "blocked accounts" to make up for their loss in value.

"Once these accounts exist, the pressure will be unstoppable from the banks for the Brazilians to change their current strict laws against foreign ownership of Brazilian companies," a consultant to Bankers Trust confided. "We will be converting our Brazilian debt into equity in the Brazilian economy."

This is precisely why Citibank, for example, has been pressuring the Brazilian government to alter local banking laws and allow foreign banks to operate inside Brazil with cruzeiro accounts.

Test cases

The attack on juridical sovereignty has already begun, in order to pave the way for asset seizures.

In Argentina, the government fought for the better part of 1983 against creditor pressure to change Article 4 of the bankruptcy code, which gave domestic creditors legal preference over foreign debt holders. In October the government finally signed the refinancing arrangement for the debt of Aerolineas Argentinas. A crucial clause in the contract essentially abolished Article 4 and granted foreign creditors, through a "cross default" provision, access to the assets of other state enterprises—the state oil monopoly, YPF, for example—in the event of an Aerolineas default.

In the Mexican case, there have been two proposals floated that would hand over Mexico's huge oil deposits to foreign banks. Long-time Moscow ally Armand Hammer of Occidental Petroleum wants Pemex, the Mexican oil monopoly, to put up its oil as collateral for all future lending and refinancing. An even more drastic version of this idea was printed in the *Wall Street Journal* last month. This plan would simply deposit Mexican oil in the U.S. strategic reserve *before* any default proceedings arose, and Mexico would be required to pay its debt directly in barrels of oil. A similar scheme for Venezuela has been drafted by Morgan Guaranty's London branch.

Brazil has already violated its own constitution to satisfy creditor demands that it surrender sovereignty. A clause in the so-called Project 2 contract signed in February of this year submits the Banco do Brasil to the jurisdiction of New York and London courts in the event of default. The guarantor of the agreement is the Central Bank, an entity of the central government, which, according to Brazilian constitutional law, cannot submit to foreign jurisdiction.

In Peru, as a result of a program administered by Wells Fargo and the World Bank, over 150 state entities have already been sold to private interests as a first step toward turning sovereign assets over to the creditors.

Figure 3
Currency devaluation
currency units per dollar

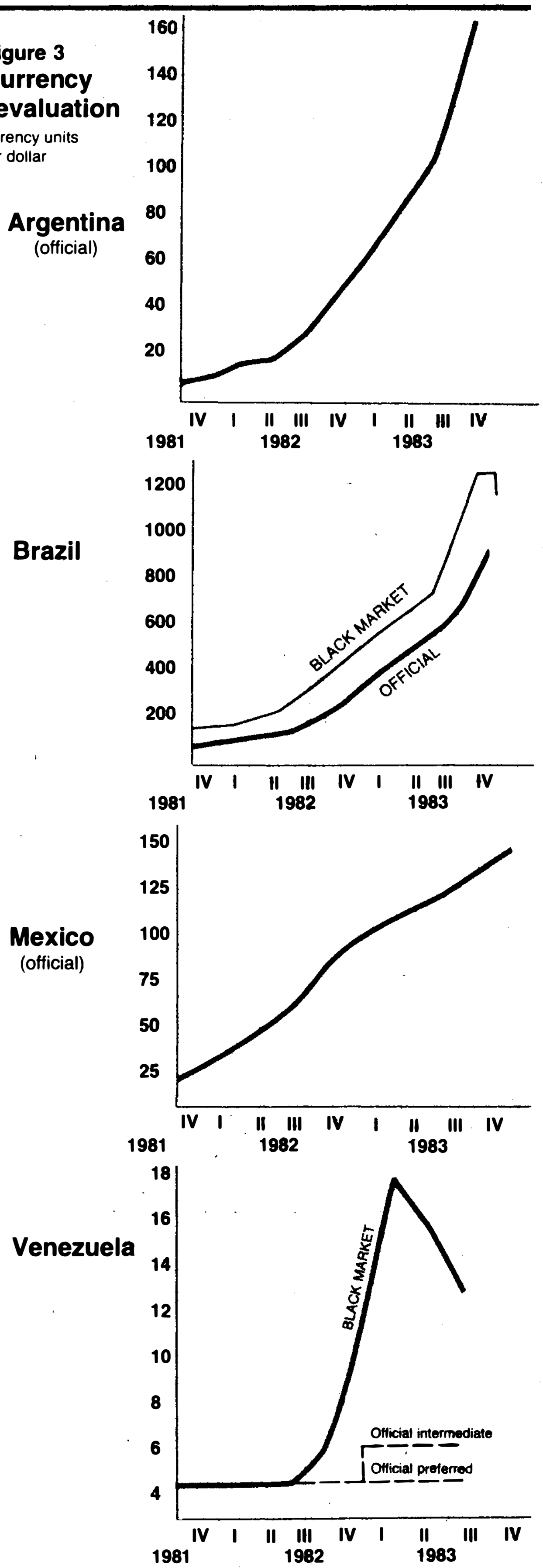
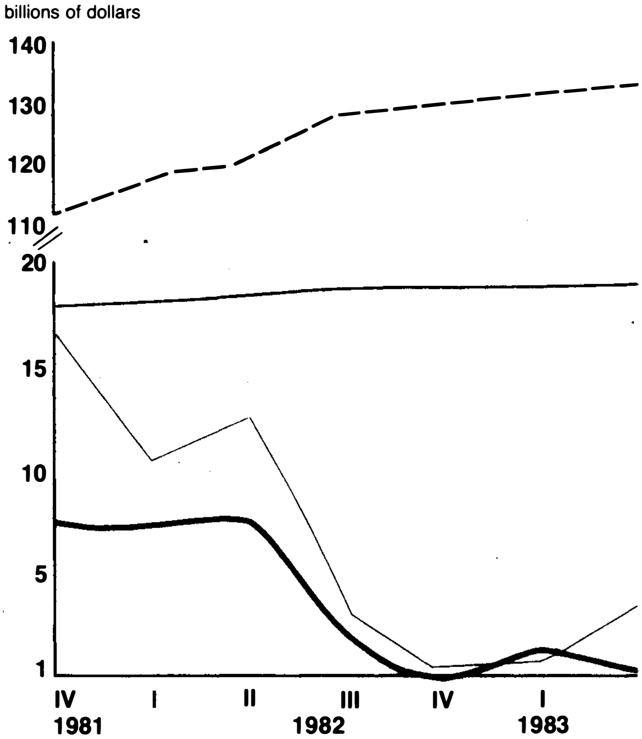


Figure 4
The collapse of lending to the Third World



New Euromarket loans to Ibero-America
New Euromarket loans to LDCs
Citibank total loans outstanding
Citibank loans outstanding to Ibero-America

Fed tries coverup of banks' bad loans

The deliberate financial upheaval of the last two years orchestrated by the creditors' conspiracy has bankrupted not only the debtors, but the banks of the creditor countries as well. American banks have been used the way Nazi Economics Minister Hjalmar Schacht used the German central bank: as shells used to loot the debtors' economies.

One bank analyst estimates that U.S. banks now hold at least $100 billion in Ibero-American loans. Asked privately how much of that is non-performing at the moment, he replied: "all of it." The top 18 banks in the country hold about $70 billion of that bad debt, he added.

These "non-performing loans" are in excess of the total capital of these banks—a flagrant violation of U.S. law and a fraud against the banks' capital holders. The regulatory agencies of the U.S. government know it, and are covering it up. In September Federal Reserve Chairman Paul Volcker permitted a 90-day "stretch-out" of loans to Ibero-America. But that grace period expires in December, threatening to bring the crisis to a head again. Obligingly, the Federal Accounting Standards Bureau intervened to legalize the Fed's action, by allowing banks to keep bad assets on the books.

The Controller of the Currency, C. T. Connover, is threatening to resign. If the banks go broke, the Fed's violation of the law will be out in the open for all to see.

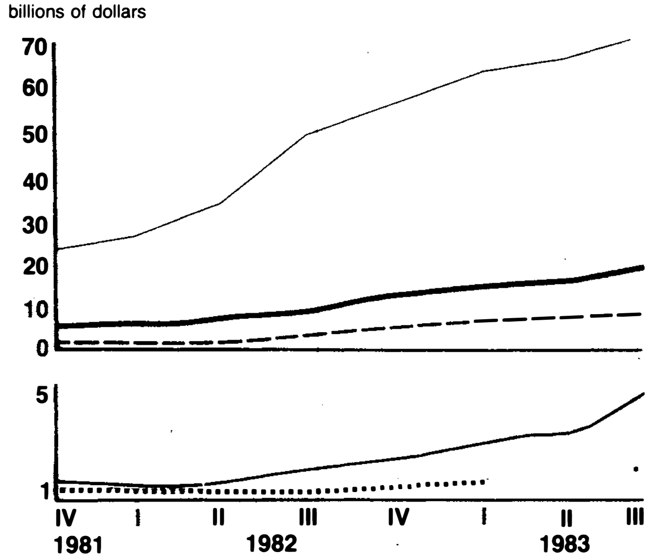
The trouble is beginning to show up even in the official figures (see **Figure 5**). The officially listed non-performing loans of major U.S. banks rose sharply in the third quarter of this year. Total non-performing loans, both foreign and domestic, of the top 18 banks rose to some $20 billion officially reported at the end of September, from about $18 billion at the end of June, according to estimates based on a study of 16 banks by Warburg-Parisbas-Becker bank analyst George Salem.

Out of the $20 billion total, the top 18 banks have at least $8 billion in bad foreign loans, mostly to Ibero-America, which they are officially admitting.

The official figures "are going to get a lot worse in the fourth quarter," a Chicago banker warned. "During the third quarter most banks actually declared minimal losses. Brazil, Argentina, and Mexico all made tiny payments to make it look like they were not 90 days behind."

As *EIR* reported in our Dec. 6 issue, Bank of America in particular seems to be trying to force the issue of the bad loans, evidently in hopes of bringing about a "new Bretton Woods" reorganization of the world debt system. While Citibank is reporting only $2.6 billion in bad loans for the third quarter, Bank of America reported a total of over $5 billion. Bank of America is reporting foreign bad loans for the quarter of some $2.3 billion, compared to Citibank's report of only $2 billion foreign non-performing loans. Citibank is $10 billion larger than Bank of America.

Figure 5
Non-performing loans by U.S. banks



Actual non-performing loans to Ibero-America at top 18 U.S. banks (*EIR* estimates)
Official non-performing loans to all borrowers at top 18 U.S. banks
Official non-performing loans to Ibero-America at top 18 U.S. banks
BankAmerica: official non-performing loans to all borrowers
Citibank: official non-performing loans to all borrowers