Ecuador Declares Partial Debt Moratorium

by Dennis Small

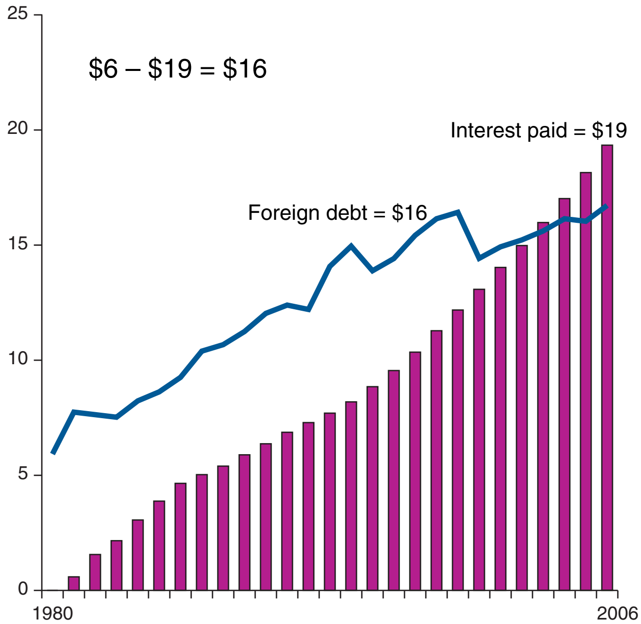
Ecuadorian President Rafael Correa announced on Dec. 12 that his government would intentionally default on $3.8 billion in government bonds held by foreign financial institutions—i.e., the country's sovereign debt. This is 39% of the government's total foreign debt, which also includes $4.3 billion owed to multilateral agencies such as the Inter-American Development Bank, and $1.5 billion in bilateral debts to countries that are not affected by the announcement.

"I have issued orders that interest payments not be made, so the country is in 'default' on its foreign debt," Correa announced. "We accept full responsibility for this fact."

On Nov. 20, Correa had warned that he did not intend to pay the foreign debt, because it was "illegitimate, corrupt, and illegal," according to findings issued that day by the Commission for the Full Audit of Public Credit (CAIC), which the government had convened in July 2007 to conduct the audit. The CAIC, composed of respected international economists and legal experts, found that the foreign commercial debt had functioned as an illegitimate and illegal looting mechanism between 1976 and 2006, rising from $16 million in 1976, to $4.2 *billion* in 2006, despite the fact that there was a net transfer to the creditors of $7.1 billion in interest and principal payments over that 30-year period.

EIR has frequently referred to such looting schemes as "bankers' arithmetic:" in this case, 0 – 7.1 = 4.1. For example, *EIR* presented **Figure 1** a few years back, employing somewhat different categories (Ecuador's total foreign debt, public and private), to demonstrate such "bankers' arithmetic." More broadly, for decades *EIR* founder Lyndon LaRouche has denounced the illegitimacy of most developing-sector foreign debt as exemplary of the global speculative bubble of financial assets which can never be paid. The total official foreign debt of developing nations today comes to about $2.5 trillion—which is a mere 0.1% of the total financial bubble of some $2 or $3 *quadrillion*. But it is a characteristic microcosm of that mega-bubble, and it directly affects the very existence of sovereign nation-states.

FIGURE 1
Ecuador: Bankers' Arithmetic
(Billions $)



Source: EIRNS.

The Correa government seems generally aware that the global crisis must be resolved, if there is to be any hope for a small country like Ecuador—although his government has also been susceptible to the British-sponsored trap of promoting regional currency blocs as a viable alternative, which it is not. But on Nov. 20, Correa stated that "there will be no unified solution to the problem of foreign debt, if the international financial architecture is not reformed. . . . The contribution of the government of Ecuador to achieve this objective begins by determining that the foreign debt is illegitimate and promoting the creation of an International Arbitration Tribunal for the Foreign Debt."

Similarly, in a discussion with *EIR* on Nov. 22, Ecuador's Minister for Economic Policy Coordination, Pedro Páez explained:

"It is necessary that the multilateral financial institutions of the United Nations system, the Paris Club, and the governments themselves of the countries of the North, demand audits of the foreign debts of all the countries. . . . If they didn't do anything wrong, what are

Presidendia del Republica del Ecuador

Ecuadorian President Rafael Correa (right) announced that the nation will not pay the portion of its country's foreign debt which is "illegitimate, corrupt, and illegal," according to the findings of a government-commissioned audit.

they afraid of? Everyone should do the same thing [that we did]. It is possible that the same thing will be discovered in other cases, because it's the same kind of actors, in the same circumstances, with the same financial instruments."

Correa has also argued, and rightly so, that the "servicing of the debt must take into consideration the consequences of that servicing on the general welfare of the Ecuadorian people."

A number of representatives of the Ecuadorian government, including Páez, have deployed across South America and abroad to argue their case, and urge other nations to conduct similar audits.

Usury Unmasked

The exhaustive CAIC study is useful in that it documents one concrete prototypical case of the illegitimacy of debt instruments in today's bankrupt system. For example, U.S. Federal Reseve Chairman Paul Volcker's 1981 raising of interest rates up to 21%, drove Ecuador to default on debt it had contracted at 6%, and the ensuing refinancing operations capitalized the unpaid interest into an unpayable mountain of new debt. The CAIC did a projection which shows that, had interest rates remained at 6%, Ecuador would have entirely paid off its public commercial debt by 1995, and that it has paid an additional *$5.4 billion* since then. Instead, Ecuador today stands saddled with $4.2 billion that it supposedly still owes.

That Volcker-induced bankruptcy also led to an International Monetary Fund and creditor bank plan, under which the government of Ecuador was forced to assume responsibility for about $1.5 billion in *private* sector debt to those banks, in an arrangement known as *sucretización.* Under the plan, the private sector was allowed to issue payments on its foreign debts in sucres (the local currency) at a fixed, low exchange rate, which the government then had to convert into dollars with which to pay the foreign banks, as the value of the sucre plummeted. In other words, the government simply took over the private sector's foreign obligations, at the creditors' insistence.

Numerous other irregularities and illegalities are documented by the CAIC, such as the 1992 Tolling Agreement, under which Ecuadorian negotiators signed a document renouncing the country's right to the prescription (termination) of existing debt after six years of non-payment, which the CAIC explains is *non-prescribable* according to the Ecuadorian Constitution and other laws. Likewise, the 1995 Brady Plan reorganization of the foreign debt took $2.5 billion in overdue interest payments, and capitalized it into new debt on which interest was then charged—anatocism, which is expressly illegal under Ecuadorian law.

Ecuador's debt moratorium is the first such move since Argentina's December 2001 sovereign default, in which President Néstor Kirchner steadfastly refused to knuckle under to the vulture funds. In the Ecuador case, the international financial predators have already begun to issue threats, as reflected in a Reuters wire which discussed "possible scenarios that Ecuador could face," including seizure of Ecuadorian assets or freezing of bank accounts abroad; oil companies and other foreign investors cutting back on investments; and all of this could "trigger political instability in a country where the last three presidents were toppled by street and Congressional turmoil."

The predators' concern is not about Ecuador's debt as such, but about the precedent being set for the rejection of the entire international financial bubble, both because of its violation of the natural law principle of the general welfare, as well as of specific national laws.