The BIS and the Brazilian bridge loans

by David Goldman

Bank for International Settlements President Fritz Leutwiler has been playing a game of brinksmanship with the world financial system which has aroused tremendous anger against the Swiss in Washington as well as London.

A Federal Reserve official claimed March 15 that on March 6 Leutwiler attempted to force collection of the $1.45 billion in bridge loans owed to the BIS by Brazil, the top debtor nation. Leutwiler, the Fed source stated, ignored last-minute pleas from the Brazilian central bank for a few more weeks', or days', grace, and forced the repayment.

The U.S. Treasury, the Fed official said, is under the influence of Swiss-style free marketeers, such as Undersecretary of the Treasury Beryl Sprinkel and Milton Friedman, and has also demanded, and received, payment in full of a $400 million bridge loan to Brazil. The uproar in Washington over the "bankers' bailout" made it "too politically explosive" for any of the monetary authorities to hand additional money to Brazil, he explained. "The bankers got themselves into this mess and now they're stuck with it," the Fed official said. "We're not going to bail those bastards out."

A Treasury official responsible for Brazilian payments, however, denied the Fed's charges, and accused both the Swiss-based BIS and its Fed collaborators of "lying and spreading panic" throughout the international financial markets. "The Fed is crazy," he said. "I'd have been called up and told in the middle of the night if the BIS did anything like this. The U.S. government has backstopped [guaranteed] $500 million of that $1.45 billion BIS loan," he fumed. "So I'm owed $500 million of it. If Leutwiler wants to call it in, he has to ask me, as one of the creditors, first!

"Leutwiler is spooked by the state of the financial system," the Treasury official continued. "The Swiss are scared, they're terrified. Leutwiler can't handle it. He's burnt out, this is a classic case of burn-out, he can't take the 15-hour days holding the system together. Bad case."

Treasury claims that the BIS had indeed refused urgent requests by Brazil to postpone a $400-million installment payment due March 6 on its $1.45 billion loan, which was scheduled to be repaid at $400 million per quarter. The Brazilians have made that payment under pressure, he said. "The U.S. government has not denied any request by Brazil for additional funds," the Treasury man also insisted. "There is no shift in the attitude of the U.S. authorities."

Debt moratorium: front burner

Whoever is telling the truth among the thieves, "the whole refinancing operation has been an exercise in futility," said a senior U.S. government official involved in the negotiations. He was referring to the entire Brazilian bailout hammered together by commercial banks and the International Monetary Fund earlier this year. "Now Brazil is back to square one. They don't have the money they need to finance their deficit for the rest of the year, and they will start going into arrears on their debt payments to the banks." Brazilian businessmen have told *EIR* that "the idea of simply declaring a debt moratorium is growing every day," as one influential industrialist put it. "We are studying the cost of not paying and suffering the consequences, compared with what we are paying under the IMF now."

Asked about U.S. economist Lyndon LaRouche's proposal for an Ibero-American common market, he said, "We are now studying this scenario carefully as well. There is a grouping that thinks we should unite the debtors and provoke a confrontation. Under the present circumstances, I don't think we'll last another two months."

The Reagan administration, meanwhile, is paralyzed by the insistence by Secretary of State George Shultz and Treasury Secretary Donald Regan that the crisis is over. "The thing is not a temporary problem, it's a systemic crisis," exploded one senior administration official. "Secretary Shultz knows this, although he's playing cagey. [Fed Chairman Paul] Volcker knows it. But the Treasury is just denying there's any problem at all, and they're in charge of it!"

A senior State Department official explained why the crisis has not been officially acknowledged. George Shultz, he said, "is aware that there is a full systemic crisis in the international banking system. But if we said so, it would just be playing into the hands of those in the governments of Brazil, Argentina, and Venezuela who are calling for joint debt moratoria. It is clear from the New Delhi summit and the preparations for UNCTAD in June that . . . [many] of these governments want this, although it has not become government policy. . . . I'm talking about foreign ministers and people in the foreign ministries. . . . The U.S. government simply can't announce it's a systemic problem, because then the debtors will come up and say, 'Fine, we have a solution: Write if off! . . . They are not just talking about rescheduling as we now have it. They want an actual reduction in payments they must make—whether some of the value of the debt is written off, or they have moratoria, whatever. Furthermore, they are not fond of the IMF system, where they have to go to the IMF and to the banks and justify themselves and beg. They want a political alternative in which they have more control."

"Our strategy," the official said, is to "use the finance ministers," the bankers' protégés, to control the situation. "They are the only ones who understand the world financial system. So far, our approach has worked. As soon as some other minister starts calling for a debt moratorium, the finance minister comes out and shuts him up, pointing out that he needs to be able to work with the IMF and the banks.

On March 3, Jacques de Larosière, managing director of the International Monetary Fund, had told a Swiss audience, "Analysis reveals that there does not exist a global debt crisis, [and] that current liquidity problems can be resolved." In a speech entitled, "The IMF and the Developing Countries," de Larosière claimed: "earlier fears have not been borne out, and the system has shown both its resilience and its adaptability. . . . Adjustment is underway throughout the world economy and confidence is being rebuilt." The State Department official, in effect, termed de Larosière a liar.

BIS-IMF coup in Washington

The Bank for International Settlements meanwhile is moving to use the crisis to extend its control over the Fed to control over the government of the United States. In the Senate Foreign Relations Committee on March 16, Sen. Charles Percy (R-Ill.), the committee's chairman, introduced a plan to "study" American entry into the Bank for International Settlements. Rejected by Congress when the BIS was founded in 1931, the plan to bring the United States in has been revived by Morgan Guaranty Trust's Rimmer de Vries. Since the BIS, unlike the International Monetary Fund, is a private Swiss-based bank responsible to no government, such action would compromise American sovereignty.

There would be "absolutely no political resistance in . . . Congress to U.S. participation in the BIS," he asserted. By a vote of 14 to 3, the Senate Foreign Relations Committee passed March 16 the IMF quota increase bill (S.659), with Percy's BIS amendment, he noted (see Congressional Closeup). "All this stuff in the *Wall Street Journal* about congressional resistance to the IMF is nonsense. The IMF will have very little actual voting resistance."

The Bank of England is meanwhile using the crisis to push for more power for the IMF. On March 15, the London *Financial Times* reported the Bank is a supporter of plans by Lazard Frères banker Felix Rohatyn to use the crisis to set up a global version of New York's Municipal Assistance Corporation, the austerity enforcer which collected the city debt.

From the March 15 London Financial Times:

The idea of a new international banking lifeboat has generated much discussion among bankers and several rough proposals. Three of the most talked about come from Barclays Bank, from the chairman of Morgan Grenfell and from Mr. Felix Rohatyn, chairman of New York's Municipal Assistance Corporation, and a partner at Lazard Frères.

Mr. Timothy Bevan, Barclays chairman, last week threw his weight behind a plan for a "rediscounting facility" which would enable central banks to provide liquidity relief for banks with problem loans, although not actually to transfer risk.

Mr. Peter Leslie, senior general manager at Barclays Bank International, feels that within the next six months the world's banking system will need to cope with the "secondary effects" of the international debt crisis—a continued slowdown in growth and even a possible reversal in Euromarket lending, in both the interbank (bank-to-bank) market and in the area of direct lending.

He fears a liquidity problem as banks with a "heavy weight of immobilized debt" shy away from new loans. If banks have a sizeable part of their loans "locked up" as a result of debt rescheduling agreements which provide for repayment of interest only and not principal, they will find "3,000 reasons not to lend any more," according to Mr. Leslie.

His answer to this problem is for central banks to agree to purchase portions of such loans from banks, at a discount, as a temporary relief measure. In exchange, the banks must agree to lend the equivalent amount in new money, perhaps as export credits.

If the discounted loan turns sour, it will revert to the bank, which will then have to write it off. If the loan matures then the central banks will collect the principal, having already provided cash to the banks for the discounted loan.

Like Mr. Leslie, Mr. Bill Mackworth-Young of Morgan Grenfell stresses that his plan is only in very rough form. "The basic thrust of all these plans," he explains, "is to strip assets out of the banking system which shouldn't have been there in the first place."

Mr. Mackworth-Young would like to shift the burden of problem bank assets from the banking system to the international capital markets. His scheme is to create a new agency, supported by the IMF or central banks, which would purchase bank loans at face value and issue in exchange non-interest bearing bonds. This paper would then be discountable at central banks if serious liquidity problems arose.

In addition, these central bank-backed bonds could be converted into a second type of paper, which would carry a low interest coupon and would be tradeable on a new secondary market.

The Mackworth-Young plan then provides banks with two options: either to hold the face-value bonds and not write down the loans, or to write down the loans and dispose of the paper on a new secondary market. The secondary paper would be guaranteed by central banks, making it, in Mr. Mackworth-Young's view, the equivalent of "Quadruple A Paper."

Mr. Felix Rohatyn also favors the creation of a new agency, possibly a World Bank or IMF subsidiary, which would issue banks with long-term low-interest bonds in exchange for dubious loans. But he points out that the political difficulties of such a program are "immense."

Mr. Rohatyn is aware of the prospect of an outcry against "bailing out the banks" but suggests that some kind of scheme is vital in order to ensure a "strong and healthy banking system."