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Debt and Ibero-America's trade

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We present below the first installment of a study of prospects for Ibero-American economic integration, which will appear in full in *EIR*'s fall and winter 1985 *Quarterly Economic Reports*. The present study comprises the first complete evaluation of what has happened to Ibero-America's trade position as a result of the debt crisis. The results run totally contrary to the version presented by the International Monetary Fund and related agencies.

First, Ibero-America's terms of trade with respect to the United States, as measured by a basket of 37 commodities studied by *EIR*, fell by 35.2% between 1980 and 1983. This figure is derived by dividing American imports from Ibero-America, as measured in tons, by the corresponding dollar price figure, as reported by the United Nations. This simple and irrefutable method of calculating export prices has not occurred to the International Monetary Fund, which asserts that Ibero-America's terms of trade worsened by only 12.9%.

Secondly, Ibero-America underwent a drastic change in export profile, from an exporter of raw materials, to an exporter of industrial manufactured goods, especially energy-intensive, capital-intensive intermediate goods. The myth of Ibero-America as a backward source of raw materials for the industrial West is refuted by this trade profile:

EIR's basket of 19 energy-intensive intermediate goods showed an average increase of volume of 153.2% over the three-year period. Prices for the same commodities declined by an average 34.9%.

On the contrary, *EIR*'s basket of 18 agricultural and mining commodities showed a *decline of export volume* of 28.75%, with the largest decline registered in the traditional sources of Ibero-American foreign exchange, i.e., the mining commodities. *EIR*'s basket of eight primary-mineral commodities registered a 34.5% decline, or 20% higher than the average decline. For the raw materials group as a whole, export prices declined by 35.4%.

The price decline of 35.2% during the 1980-83 period, i.e., the worst ravages of the debt crisis, does not, of course, fully estimate the undervaluation of Ibero-American currencies. In market-basket terms, all such currencies were underpriced by 20-30% against the American dollar, before the debt crisis exploded after 1980. The true undervaluation of Ibero-American currencies, therefore, lies in the range of 55-65%.

Finally, the cost to these countries due to the collapse of export prices, which represents a cost of the debt crisis, must be added to their reported interest bill, in order to measure the cost of International Monetary Fund usury. The result is startling: As of 1983, the last year for which we have complete data, Ibero-America paid an effective interest rate of 24%.

These results are summarized in **Table 1.**

The great resource grab

The form in which the United States has parasitized the resources of Ibero-America is made clear in **Table 2**, which matches American imports of refined metals to imports of the corresponding ores. In most of the ore categories, the results show a major decline in export volume, whereas all of the refined metals show spectacular increases. Steel is a case in point: American imports of iron ore from Ibero-America fell by 63% during the debt crisis, while imports of finished steel rose to 2.454 million metric tons, or about 15% of total American steel imports, and 3% of total American steel consumption. Another is aluminum, exports of which rose, in volume terms, by 135%, while U.S. imports of bauxite and alumina fell by 53%.

Ibero-American government ministers who have long suspected that something else than free-market forces were at play in the commodity markets will find the comparison of price declines in the two market-baskets of enormous interests. Most of the items in the raw-materials market basket are sold in dollars, according to the vagaries of the commodity exchanges; almost all of the items in the intermediate-goods market basket are sold in national-currency terms. The above results show that the price declines in the two categories—one brought on by falling commodity-market prices, the other by International Monetary Fund-imposed currency devaluations—are virtually identical.

That is not surprising, since the commodity price-declines, as well as the currency devaluations, are the result the same global credit squeeze, imposed upon the developing world by the International Monetary Fund and the Bank for International Settlements.

However, the results, as such, show up for a miserable sophistry the International Monetary Fund's argument that currency devaluations will lead to higher exports. The in-

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Table 1

Ibero-American trade with the United States, 1980-83

(Percent)

Commodity	Price change	Volume change
Industrial intermediate goods		
Refined lead	−55.6	19.9
Refined zinc	−11.1	21.6
Aluminum	−41.7	135.4
Refined nickel	−75.0	7.2
Refined copper	−27.3	47.5
Iron steel wire	−54.5	485.5
Iron strip and hoop	−39.4	175.8
Iron plate	−26.8	215.7
Iron shapes	−43.5	122.1
Iron primary forms	−26.2	453.3
Pig iron	−49.4	154.8
Cement	−27.3	139.4
Rubber tires, tubes	−30.7	192.0
Starch inulin gluten	−31.3	4.2
Manufactured fertilizer	−35.0	419.4
chemicals	−25.0	61.5
Petroleum, refined.	0.0	−5.2
Pulp and paper	−23.5	86.2
Synthetic rubber	−36.4	174.3
Primary products (agriculture and mining)		
Tungsten ore	−52.9	−31.1
Tin ore	−25.6	−63.1
Lead ore	−22.4	7.3
Copper ore	−86.0	−29.0
Zinc ore	−55.8	−51.7
Aluminum ore	12.8	−53.2
Iron ore	−4.0	−62.8
Wool	−15.6	−60.8
Natural fibers	−27.3	−20.5
Cotton	−44.4	−34.5
Natural rubber	−30.2	−20.1
Sugar and honey	−25.0	−44.8
Vegetables, prepared	−25.0	−4.5
Fruit, nuts	33.0	−5.8
Vegetables, fresh	−28.5	18.1
Cereal preparations	14.3	−36.5
Prepared fish	42.3	−43.2
Frozen fish	−15.7	−17.7

Industrial commodities
No. commodities studied: 19
Avg. rise export volume: 153.4%
Avg. decline export price: 34.7%

Primary products
No. commodities studied: 18
Avg. decline export volume: 33.5%
Avg. decline export price: 35.4%

All categories
Avg. price decline: −32.9%

crease in Ibero-American exports to the United States is a simple function of the collapse of the American economy. As the American economy shuts down its capital-intensive, energy-intensive basic industry, it buys abroad the intermediate goods it no longer produces at home, at a fraction of the domestic cost of producing such goods. Price declines of about 35% did not help the Ibero-American countries sell more iron ore or alumina, since the United States no longer processes such goods. On the contrary, these countries found a ready market for goods higher up on the scale of processing, replacing the production whose capacity the United States has destroyed.

Upon the $360 billion in debt shown outstanding in **Table 3**, Ibero-America's interest bill is given by **Table 4.**

The interest paid, which in 1983 amounted to 70% of Ibero-America's $68.8 billion in exports to the industrial world, does not reflect the full cost of usury imposed upon these nations through International Monetary Fund conditionalities. If the excess payments for imports, and revenues lost upon exports, are added to the interest bill reported above, the total debt service paid by Ibero-America in 1983 was $87.5 billion, and the true rate of interest was 24%.

The complete measure is obtained by adding the interest bill to revenues lost as a result of poorer terms of trade. Above, we calculated the deterioration of terms of trade to be 35.2%. Applied to Ibero-America's trade data, this yields the result shown in **Table 5.**

Treasury Secretary James Baker III's demands for "economic restructuring" in the debtor countries, under World Bank guidance, derives from plans circulated during the past two years by Henry Kissinger and his circle. The core of the plan, exchanging debt for equity shares in raw-materials and industrial capacity in the debtor countries, was first floated in a big way during a September 1982 meeting of the Aspen

Table 2
U.S. industrial vs. raw materials imports from Ibero-America
(Percent change)

Commodity	refined metal	metallic ore
Lead	19.9	7.3
Zinc	21.6	−51.7
Aluminum	135.4	−53.2
Nickel	7.2	n.a.
Copper	47.5	−29.0
Total iron and steel	360.7	−62.8
By category:		
Steel tubes	50.1	
Iron Steel wire	485.5	
Iron strip and hoop	175.8	
Iron plate	215.7	
Iron shapes	122.1	
Iron primary forms	453.3	
Pig iron	154.8	

Institute in Aspen, Colorado. Using estimates made available by close collaborators of Henry Kissinger, we have prepared the following estimates of the scale of looting implied by the proposal.

Former Assistant Secretary of State Robert Hormats, who was promoted in the State Department by Henry Kissinger and is now Kissinger's assistant at the Goldman Sachs investment bank in New York, told a journalist on July 9, 1985 that there has been "new enthusiasm" in Washington for Kissinger's debt for equity proposal. Hormats's judgment was apparently borne out by the Baker plan offered to the just-concluded International Monetary Fund meeting in South Korea.

The plan was earlier described by Kissinger in the June 23 *Los Angeles Times* and elaborated by Hormats in Senate testimony June 24.

Hormats described the equity swap as a "great way to bring free enterprise to Latin America," which will "give foreigners eventually a 15-20% ownership stake" in what happens to Latin America.

He gave as an example the recent Goldman Sachs underwriting of a $50 million Eurodollar bond for the Panamanian government owned-bank Bladex. With this bond issue, Goldman Sachs "privatized" the government bank by selling its equity to the Eurobankers. The significance is that this was the first time in three years that a Latin American entity, either government or private sector, was able to sell a Eurodollar bond. It is a floating rate note at 1% over Libor, or 9%, and will rise as Libor rises.

According to Hormats, one-fifth of Ibero-America's debt should be converted into equity, or roughly $80 billion; the

Table 3
Total foreign debt of 9 Ibero-American countries, BIS vs. EIR
(Billions U.S.$)

	1980	1981	6/82	1982	1983	1984
Argen/BIS	20.4	22.9	23.5	22.2	27.3	25.9
BIS ratio	153%	153%	165%	165%	165%	165%
BIS (adj.)	31	35	38.7	36.6	45	42.7
EIR est.	35.7	43.0	43.0	45		
Brazil/BIS	44	49.7	52.4	56.1	71.9	75.7
EIR est.	77.2	86.1	92	100.8		
Chile/BIS	9.6	10.6	10.4	13	13.6	
EIR est.	15.5	17.3	19.1	19.2		
Colombia/BIS	4.9	4.9	5.5	7.3	6.9	
EIR est.		8.3	9.7	10.6	12.0	
Mexico/BIS	42.8	55.5	62	59	72.6	72.8
EIR est.	64.0	83	88	88		
Peru/BIS	4.3	5.1	5.2	6.6	5.8	
EIR est.	8.6	10.4	10.5	10.5		
Venez/BIS	22.3	22.5		22.6	28.0	26.1
EIR est.	30.8		34.3		34.6	34.6
Panam/BIS	25.7	25.2		27.9	31.6	30.5
EIR est.	38.6		37.8	41.9	47.4	45.7
Cuba/BIS	1.4	1.1	1.0	1.2	1.1	

	1980	1981	1982	1983	1984	1985
Debt with Panamanian foreign deposits						
Total of 9	286.1	312.8	309	375.2	371.2	
Plus Ecuador, Carribean, etc.: less than $30 billion						
Total continent	256	308	338	334	405	400
Debt without Panamanian deposits:						
Total of 9				270.1	335.2	331.2
Total continent				316	365	360

Table 4
Ibero-American debt service
(Billions U.S.$)

	1981	1982	1983	1984	1985*
Principal	316	365	360	355	350
Interest %	14	13	12	11	11
Debt service**	44.3	47.5	48.2	44.1	43.5

* Estimate
** Interest plus $5 billion/year principal starting 1984

Table 5

The debt-service costs of Ibero-America due to terms of trade, 1983

(Billions U.S.$)

Imports	44.888
Excess import payments*	15.800
Exports	68.841
Loss of export receipts*	24.232
Total loss	40.032
Plus interest paid	47.500
Total usury bill	87.532
As % of total debt	23.98% = True interest rate

* When adjusted by 1980 terms of trade yields

required yield for this equity would be 15% per annum, or higher than the present 11% interest rate on outstanding debt.

For what it is worth, Kissinger has also circulated a proposal—which has not gone far in Washington—to "cap" interest rates, which, supposedly, would reduce them from 11% to 8%.

However, this is not a cap on the total rate, but a cap on the banks' earned "spread" over the London Interbank Rate (Libor), which the banks themselves pay to get money. Currently, the banks are paying 8% for funds, charging an average 2% spread to Latin America, or a total of 10% for new loans made in 1985. Kissinger wants to "cap" the spread to 1%, which would mean 9% rates.

In sum, the financial impact would be a reduction from 2% to 1% of the spread, or a grand total of 1% reduction in interest rates.

Even supposing they decide to "fix" capped rates, the most they could shave would be 2% from the spread. In any case, the interest costs deducted from current payments would be added to the principal under the Kissinger plan.

The Kissinger plan, even in its own self-description, would be considerably worse than the International Monetary Fund's "status quo." To demonstrate this, we project interest costs to the Ibero-American debtors under present conditions of International Monetary Fund rule. We then adjust these projections to take into account:

1) The cost of paying the demanded 15% dividend on the portion of the debt converted into equity, and

2) The supposed saving due to the "interest rate cap."

Simple arithmetic shows that the debtors come out behind under Kissinger's proposal, even in simple financial terms; this does not take into account the worst aspect of the plan, namely the loss of economic sovereignty.

The figures in **Table 6** assume no repayment of principal, and 5% per year capitalization of unpaid interest, i.e., unpaid interest to be added to total debt amount. It also assumes that 2% per year of the debt, starting in 1985, will be converted to equity.

In summary, the supposed concessions offered by Kissinger and company turn out to demand a worse rate of looting than the International Monetary Fund has imposed, under present conditions. What is most disturbing about this conclusion is that it takes the mechanics of the Kissinger plan at face value, and merely computes its consequences.

In reality, the plan would be much worse: The loss of sovereignty over national policy would ruin whatever recovery chances these nations have, throwing their national industries onto the scrapheap. The damage that would be done would make the worst of the carpetbagging after the American Civil War look like a Peace Corps mission.

Table 6

The IMF status quo and the Kissinger plan

(Billions U.S.$)

	1982	1983	1984	1985	1986	1987	1988	1989	1990
The IMF status quo									
Principal	316	365	360	355	350	345	340	335	330
Interest %	14	13	12	11	11	12	15	15	15
Debt service*	44.3	47.5	48.2	44.1	43.5	46.4	56.0	55.3	54.5
The Kissinger plan									
Principal	316	365	360	371	382	394	405	418	430
Equity conversion**	0	0.5	2.0	10	17.4	25.8	33.9	42.3	51.6
Interest %***	14	13	12	8	8	9	12	12	12
Interest bill	44.3	47.5	48.2	29.7	30.6	35.5	48.6	50.2	51.6
Equity yield (15%)	0	0.1	0.3	1.5	2.6	3.9	5.1	6.4	7.7
Combined total	44.3	47.6	48.5	31.2	33.2	39.4	53.7	56.8	59.3

* Interest plus $5 billion/year principal starting 1984.

** Assumes that 12% of the total debt will have been converted to equity by 1990, starting with a 2% conversion during 1985).

*** Assumes a "most-generous-case" of subsidized lending, i.e., loans with an interest rate "cap" of 5% on new loans.