EIR Economics

Calls for New Bretton Woods mount, as crisis worsens

by Marcia Merry Baker and Gail Billington

As we go to press, finance officials from around the world are about to gather in Washington, D.C. for meetings of the Group of Seven (the pre-meeting to the May heads of state summit in England) and the interim session of the International Monetary Fund, which this year are anything but "routine." This is shown by U.S. Treasury Secretary Robert Rubin's convening of the Willard Group (also called the Group of 22), a conference of finance ministers from 22 nations on April 16, which has been specially charged to take up the world financial crisis. The existing IMF-era institutions and arrangements are failures.

As of the eve of the Willard meeting, the intensity of international discussion, debate, and warfare over what to do with the bankrupt world financial system has reached new levels, including more calls for a whole new system. Some are calling it a "New" Bretton Woods, or a Bretton Woods "II." Others propose unspecified new agencies to supersede those of the dying IMF system.

The immediate impetus to this policy fight, apart from forewarnings by Lyndon LaRouche and collaborators, who launched a "New Bretton Woods" mobilization in February 1997, is that the process of financial breakdown—unpayable debts, insolvencies, chain-reaction defaults—is growing worse by the hour.

'Bailout III' in Indonesia

The policy stand-off on how to deal with this crisis is most dramatic in the nation of Indonesia, where the IMF announced on April 8 that it has concluded new terms for its "Bailout III" package. Although details are yet to be made available, sticking to the IMF approach means the latest package is as foredoomed as was the first one, in October 1997, and the second one, in January 1998.

In Mexico, hailed by some as a model for solving the Asian debt crises, the autumn 1997 bailout-bank privatization program has turned into a spring 1998 blow-out (see article this issue).

Then, there is Japan, the second-largest economy in the world, where an accounting-leniency decree saved the day for major banks and corporations as of the March 31 end of Japan's fiscal year, but as of April 1, the financial crisis flared up all the worse. There are huge undeclared loan losses waiting to show up in May and June. Japan's physical economy is contracting at a rate that will mean a Gross Domestic Product drop of 0.3% in 1998—the first year of economic decline in 24 years, according to the April 8 economic outlook report of the Paris-based Organization for Economic Cooperation and Development. Bankruptcies in Japan in 1997 were up 30% over the year before, and hit a record high of 17,300, totalling $100 billion in losses. The rate is worse now.

In South Korea, undergoing economic shrinkage and record unemployment, there is a debt management-liquidity requirement of $80 billion, of which about $43 billion is short-term obligations, payable over the next 12 months. There is no line-up of creditors to supply this kind of money. South Korea's recent $3 billion government debt-bond issue bombed. On April 8, the South Korean government officially asked the United States for some $5 billion in backup funds.

These developments are co-factors (along with the Federal Reserve and European central banks "printing" money) in the rush of funds zooming out of Asia, and driving up Wall Street and European stock exchanges. The Dow Jones Industrial Average broke 9,000 in April; trends in Europe are epitomized by Spain's exchange, whose share valuation index is up 50% since January.

Summing up the nature of this crisis, the German business daily *Handelsblatt* warned in its lead editorial, "Japan Should

Make Bull Investors Anxious," on April 6, that there is a "crash risk, which should not be underestimated." Chief editor Klaus C. Engelen notes that the contrast between the ongoing euphoria in New York and Frankfurt, on the one hand, and the "overall weather pattern in Asia," on the other, could hardly be more extreme. The banking crisis in the second-biggest economy of the world has reached a new dimension. And this comes exactly at a point when the "over-debted tiger states Thailand, South Korea, and Indonesia are urgently requiring considerable credit assistance by the Japanese banks to stabilize their precarious economic and currency situation."

Engelen emphasizes the "never-ending series of bad news from Japan," leading now to comparisons between Prime Minister Ryutaro Hashimoto and U.S. President Herbert Hoover before the eruption of the 1930s world depression. "The threat of a Japanese collapse is now receiving utmost priority on the agenda of global crisis managers," says Engelen.

Calls for Bretton Woods

Among the latest calls for a whole new system, are those from government leaders of Italy. Prime Minister Romano Prodi said on April 7, "We must move toward a new Bretton Woods." Speaking to reporters after a heads of state meeting in Buenos Aires, Argentina, he replied to an *EIR* corrspondent's question about the prospects for the Willard Group (of which Argentina and Italy are part):

"The meeting on the 16th does not have such a far-reaching ambition as to be a New Bretton Woods. Nonetheless, it will serve to analyze the urgent and strong measures that must be taken to confront the Asian crisis. I personally believe that we must move toward a new Bretton Woods. And this has to be analyzed very carefully, because the risk level in the international monetary system has greatly increased in the recent period. But it is an issue that can be touched upon at this meeting. It has to be the object of a very serious analysis; it is not something that is going to be done at this moment."

Italian Foreign Minister Lamberto Dini is likewise speaking out. A former IMF and central bank director, Dini said in a statement published on April 6 in the *La Repubblica* economic supplement, that he is against the idea of a general IMF bailout of the Asian crisis; he suggested setting up a new institution, in order to settle debts on the principles of an orderly bankruptcy reorganization. Under the headline "The West Will Pay Dearly for the Asia Crisis—Dini: Careful with Bailouts," the Italian Foreign Minister said that the IMF intervention slowed down the Asia crisis, but that "we cannot hide it: There is something wrong." Dini continued:

"You cannot give investors the impression that, if the investment fails, a supranational body will come in, with taxpayers' money. A moral hazard has been created, and we must temper it by introducing a sort of international bankruptcy court, to establish the principle that creditors pay for failures, and that an investment has a risk factor. As with private firms: When one goes bankrupt, you list the creditors, you may reach an agreement, but no one recovers every last penny." Dini said that the Asia crisis will cost the West at least one-half percent of Gross Domestic Product. And, he added, "There is no guarantee that it might not be worse."

Another call for a new global institution to deal with the crisis has come from the UN's Economic and Social Commission for Asia and the Pacific (ESCAP). At an April 8 press conference in Bangkok, to release its annual survey of the region's economy, ESCAP called for creation of a global agency to regulate private capital flows, curb speculation, and promote the use of regional currencies to finance intra-regional trade. UN Undersecretary and ESCAP Executive Secretary Adrianus Mooy said, "The establishment of a system of global governance of private financial flows needs to be seriously considered." Under current arrangements, he said, only the borrower is disciplined. "Some form of symmetrical treatment to both lenders and borrowers should apply." Mooy said the issue will be discussed in detail at a high-level meeting of the Asian Development Bank, UN, World Bank, and IMF, in June.

The director of ESCAP's Development Research and Policy Analysis Division, Azizul Islam, added, "I would like to stress that our emphasis is not on regulation," but ESCAP's aim is to reduce the "speculative component of international capital inflows," and to increase long-term flows at the expense of short-term flows. "The objective is to change the maturity composition of inflows. It is quite possible to have a global rule with respect to such provisions," he said, adding the critical point that, "with the political will, it is not impossible to come up with such a system, such as a tax on short-term flows."

Mooy further suggested that Asian countries reduce dependence on dollars by using regional currencies for intra-regional trade and consider an Asian Fund to supplement the IMF. He pointed out that the IMF is running out of money, as a rejoinder to objections to a regional fund.

ASEM II

Controlling global speculation was also forced through as a priority international policy issue, by Malaysia's Prime Minister Dr. Mahathir bin Mohamad, at the second annual conference of the Asia-Europe Meeting (ASEM II), on April 2-4 in London. There, heads of state from 10 Asian and 15 European nations met. On April 3, Mahathir forced a last-minute inclusion into the conference's final statement on the Asian financial crisis, focussing on protecting nations from potential shocks, "including speculation-induced instability."

The overall import of the ASEM meeting, however, hosted by British Prime Minister Tony Blair, was nil. Italy's Foreign Minister Dini described it, "Don't you see? We did nothing but repeat the usual formulas." Nevertheless, the proceedings of ASEM II signal that business-as-usual is out the window, and that no such international event will dare avoid discussing in some way, the *systemic* nature of the ongoing

Australians for LaRouche

The Citizens Electoral Council (CEC), friends of Lyndon LaRouche in Australia, launched a series of campaign bus tours in the two states of Queensland and Western Australia in March, organizing for a New Bretton Woods conference and the exoneration of LaRouche. Thirty-two CEC candidates are currently running for office. Shown here is senatorial candidate Tony Drake (left), touring Western Australia in his mobile campaign office, a bright red double-decker bus, complete with bunk beds, microwave, and refrigerator.

Drake is joined by (left to right) Craig Isherwood, National Secretary of the CEC; John Watson, candidate for the House of Representatives; Trudy Campbell of the CEC in Melbourne; House of Representatives candidate Brian McCarthy; and House of Representatives candidate Stuart Smith. The campaign tours yielded 506 signatures for the exoneration of LaRouche—double the number previously collected. The exoneration petitions will be presented to the Federal Parliament and the U.S. Embassy in Canberra.

Organizers conducted door-to-door campaign tours in 11 rural communities. They report that people from all walks of life expressed frustration with the dominant political parties, and widespread fear that we are heading for a new Great Depression. In the central Queensland mining towns of Blackwater, Emerald, and Moranbah, for example, they encountered a quiet hysteria about the layoffs that are already occurring, as a result of the Asian financial crisis.

Interest in the New Bretton Woods proposal is very keen in Australia, especially since the Asian financial blowout of last fall, which hit Australia hard. Indonesia, for example, is Australia's nearest neighbor, with which it signed a security and defense treaty in 1995. As *EIR* reported last week, the Melbourne daily *The Age* on March 30 ran a commentary asking, "For how much longer will the world economy continue to limp along before the political will is created for another Bretton Woods and measures to tame financial markets?"

meltdown of the IMF-dominated world economy.

The intervention of Thailand, Malaysia, and Indonesia in the ASEM II sessions graphically forced onto the table the devastating economic, political, and human penalties paid by these countries during the last nine months, severely contradicting the air of "feel-good, getting to know you" consensus that Blair's "Cool Britannia" theme tried to maintain.

In advance of the meeting, Thai Prime Minister Chuan Leekpai chaired a gathering of the Asian participants, with the intent to insist that the ASEM II meeting issue a separate statement on the importance of the Asian crisis, with special emphasis on the role of currency speculation as a leading cause of the crisis. The Asian group also urged that the meeting as a whole support tangible measures to provide emergency bank and credit facilities and debt relief for those countries most hurt by the crisis, and to refrain from a resort to measures to block trade.

Shortly before departing for London, Prime Minister Chuan said, in an exclusive interview with Agence France Presse, that while Thailand is fully committed to meeting the terms of the IMF restructuring package imposed last year, "at the same time, we realized that we are not fully ready for full globalization and liberalization, and, therefore, we have to take measures to protect our people from its full impact."

Saving nations, not banks

The theme of "saving the nations, not the banks" emerged as the focal point of the most important debate during the ASEM II meeting, which, in some respects, reflected a pitting of Asian "debtors" against the views of their European "creditors." As the Thai delegation, led by Prime Minister Chuan and Deputy Prime Minister Supachai Panichpakdi, repeatedly stated at the conference, European financial institutions have the largest loan exposure in Asia—at $350 billion, greater than Japan and the United States combined. In his interview and later remarks, Prime Minister Chuan stressed that debt rollover and restructuring by these creditor institutions would be among the most important "support" needed.

The conflict over international finance was most clearly evoked at a pre-meeting of businessmen representing the member Asian and European nations. Thai Deputy Prime Minister Supachai called on Europe to get more involved in devising effective means of financial surveillance and developing "early warning" systems to detect crises, along the lines of the so-called "Manila Framework" adopted at the Asia-Pacific Economic Conference summit last November. He specifically charged that "overlending" has been a major cause of the "Asian contagion," and that creditors had invented all kinds of financial instruments to further indebt Asia when the creditors' existing surveillance should have warned them of the dangers. Trade financing, he stated, is most urgently needed now, "to keep economies in East Asia alive." And, as to all the press hype about the Asian "miracle" of the 1980s, Supachai stole a line from Winston Churchill, "We know as Asians how much blood, sweat, and tears we have put in."

British Trade and Industry Minister Margaret Beckett responded to Supachai's remarks by calling for more of what the Asians objected to, more "commitment to market liberalization."

At the heads of state level, this debate was taken up in a one-two presentation by Malaysia's Prime Minister Mahathir and Prime Minister Chuan. Dr. Mahathir detailed the cost of the financial collapse in Southeast Asia, and Chuan situated that crisis in the global context. Dr. Mahathir reported that Malaysia, which was *not* the nation worst affected, suffered a 60% currency devaluation and lost $200 billion. "If you consider the number of Asian countries experiencing currency devaluation, you may be able to appreciate how much wealth and purchasing power has been destroyed," he said.

This intervention, supported by the Indonesian delegation, succeeded in inserting into the final statement a specific attack on currency speculation as a major triggering cause of the Asian crisis, which was reportedly supported by French, Belgian, and Italian participants, and evinced a split among European leaders. French President Jacques Chirac declared, "We see that the more open the international monetary system becomes, the more its fragility becomes a problem. It is not a question of regulating the international monetary system, but of strengthening it, to increase its stability and reduce the erratic behavior of markets. . . . We must not delude ourselves. If Asia suffers today, then Europe will suffer tomorrow."

At a press conference following the ASEM II meeting, German Chancellor Helmut Kohl declared, "There is no magic cure. . . . International capital flows will not obey legislation or political orders." Dr. Mahathir countered bluntly, that if the political will to do so exists, "everything is feasible."

Indonesia facing 'IMF III'

A continuing critical test of the credibility of the IMF system is what is now called Indonesia's IMF III, the third "restructuring" program since Halloween 1997. After three weeks of intensive negotiations with IMF officials in Jakarta, Indonesia's Coordinating Minister for Economics, Ginandjar Kartasasmita, held a press conference in Jakarta on April 8 to announce that a new accord had been reached. However, 24 hours later, when the details were to be released, the government put off the announcement until April 13.

At his press conference, Minister Ginandjar said that "IMF III" differs from the previous programs in three ways: First, a strict compliance regime will be imposed; second, the plan was subjected to full cabinet discussion, which was not true in January; and, third, the subject of $74 billion of private sector foreign debt has been incorporated into the package, under IMF supervision. As reported so far, the new package includes 117 specific points, each with a precise timetable for compliance. Based on previous packages, 46 of those elements have been met. The major concession, though the IMF will not admit this, has been in the area of government subsidies for essential commodities. The government will retain subsidies for rice, and fuel and energy price increases, due to take effect on April 1, will be imposed gradually according to a timetable to be worked out. All other subsidies will be phased out by October 1998.

It is far too early to evaluate the new plan, but it is already clear that the IMF will play hard ball with Indonesia. First Deputy Managing Director Stanley Fischer told a Tokyo press conference on April 8, "We will simply have to see if the system as a whole is capable of implementing the reforms. . . . It is impossible for us to go ahead 'no matter what.'. . . We have measures in place, and if they are not implemented, the program won't go ahead."

For his part, Minister Ginandjar stated clearly that no one should doubt Indonesia's determination to reform its economy, and that will occur, he stressed, "with or without" outside intervention. The touchstone of the success or failure of "IMF III" will most likely rest in the outcome of talks with the 13-member foreign financial institutions which are owed $74 billion, of which $35 billion that is owed by Indonesian firms and held in commercial papers is of immediate concern. Ginandjar described the current state of affairs on this debt as "not a moratorium. But it's often called a stand-still." The IMF and Indonesia have stated clearly there will be no government assumption of the private sector debt. Ginandjar added that creditors must give a "sufficient" grace period, especially on principal payments. A shakeup of the creditors' committee in early April strongly suggests that the Clinton administration has developed a heightened appreciation of the strategic importance of Indonesia and its economic health. The British head of the creditors' committee, David Brougham, executive director of Standard and Chartered, has been replaced by a three-member co-chairmanship, representing Japanese, German, and American banks. The next committee meeting will take place in New York on April 15. Whatever comes out of those talks, any agreement will now have to be approved by the IMF.