Thoughts after the 1980s sovereign financial crisis

Intervention in the CEPAL conference,
"La crisis de la deuda 30 años después".
Ciudad de México, February 18-19, 2013.

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This conference could be a moment for recollections

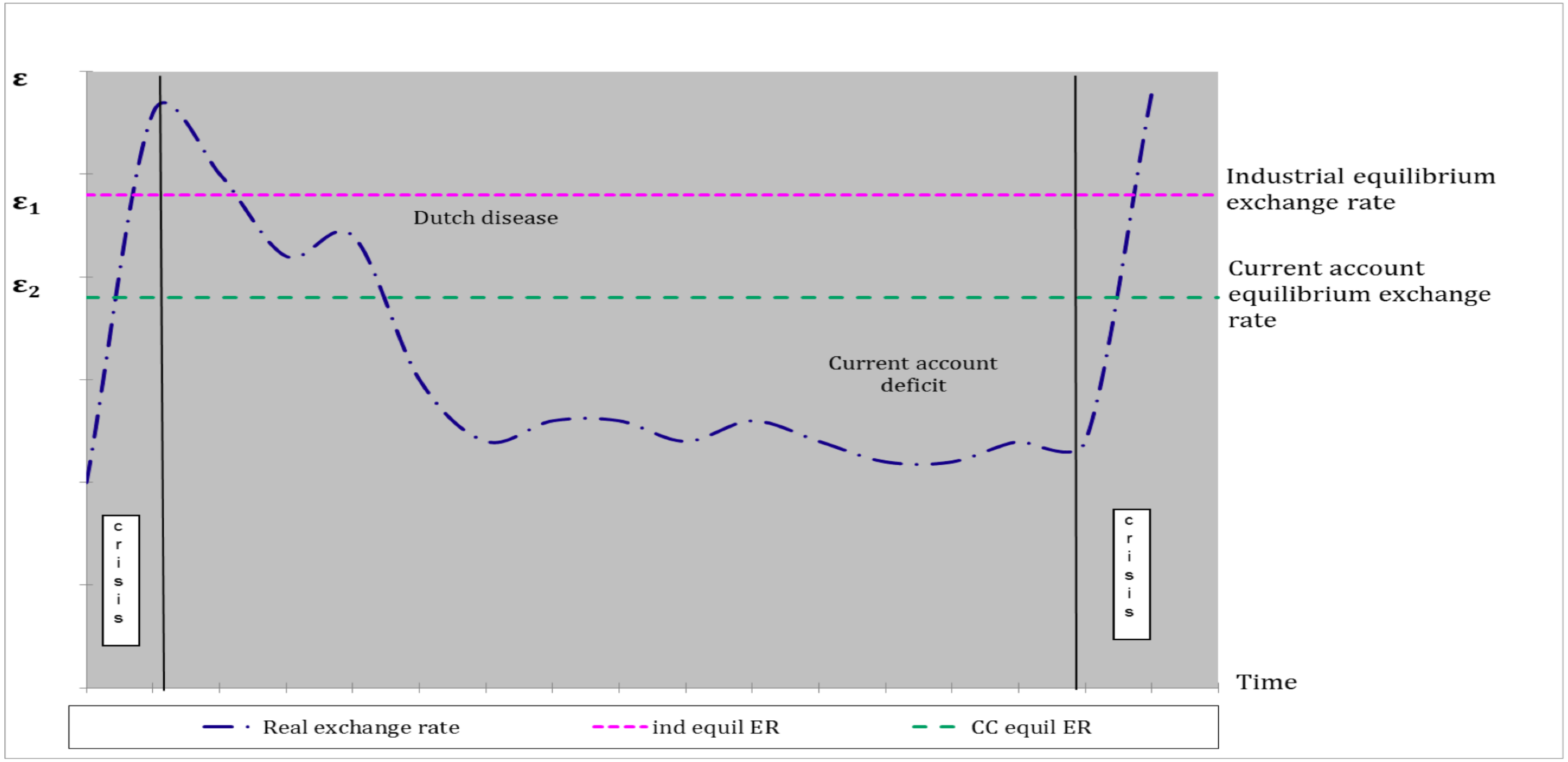
of a financial crisis in which I was an actor

- How strongly the rich countries got together
- How biased in their favor the World Bank and IMF have been
- How the Brazilians and the Argentineans got together
- How aggressively James Baker reacted in September 1987 to the Brazilian proposal on the securitization of the debt.
- How, 18 months later, this proposal became, letter by letter, the Brady Plan.

But, instead, I will discuss some often ignored issues

- The 1980s' stagnation was the outcome of a major financial crisis, not of the exhaustion of the import substitution model.
- The over borrowing involved was not consequence of populism, but of the tendency to the cyclical and chronic overvaluation of the Latin American currencies.
- This cyclical tendency is consequence of the growth *cum* foreign savings policy.
- Such policy is much more on the interest of rich countries than of developing countries.

Tendency to the cyclical and chronic overappreciation of the exchange rate



Latin American countries go from sudden stop to sudden stop

- In the late 1970s, a wave of foreign indebtedness,

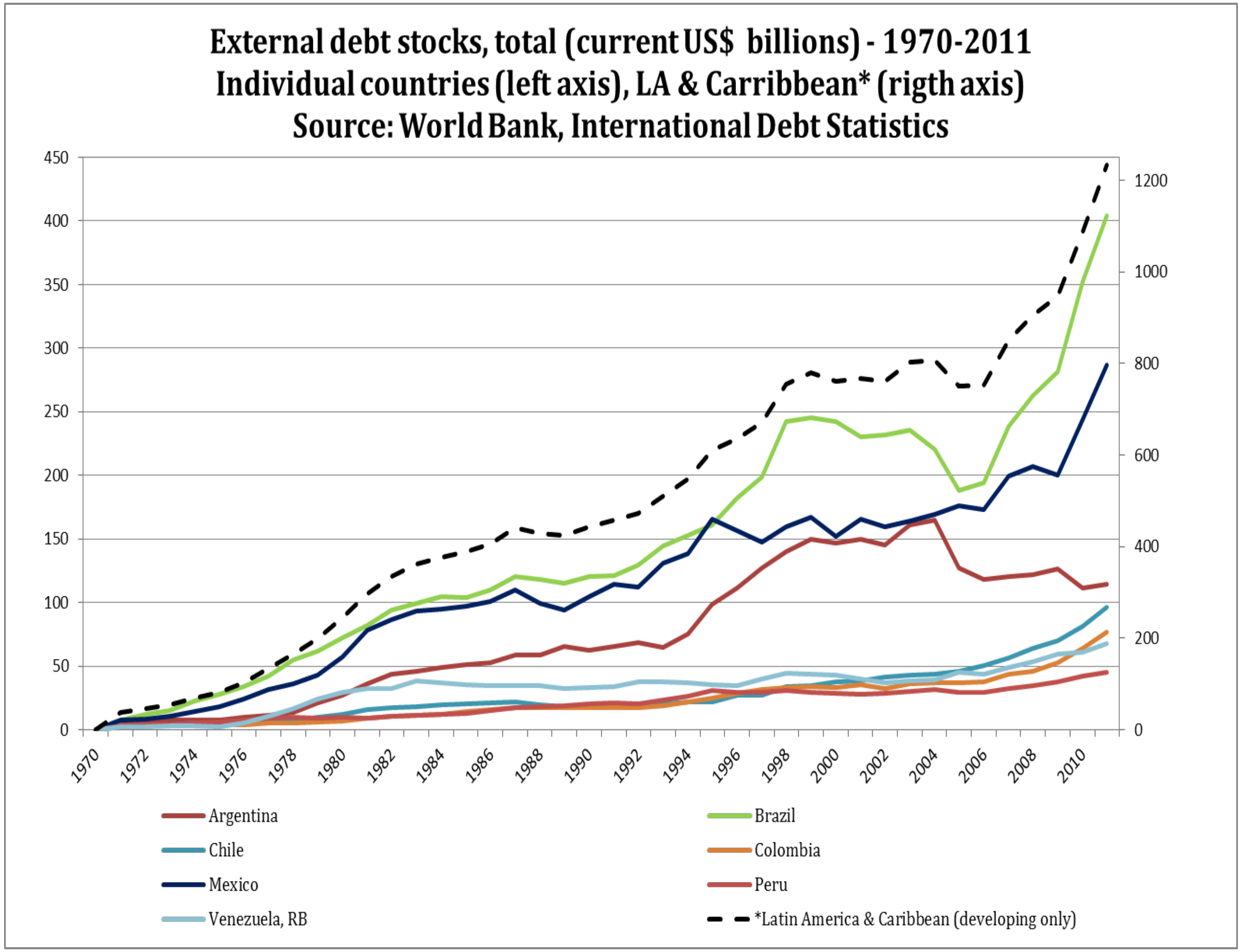
  –in the 1980s, financial crises

- In the early 1990s, a new wave of foreign indebtedness,

  –in the late 1990s and early 2000s, crises

- In the mid 2000s new indebtedness,

  –but the surge in commodity prices is postponing the financial crises (while deindustrializing or stoping industrialization).


External debt stocks, total (current US$ billions) - 1970-2011
Individual countries (left axis), LA & Carribbean* (rigth axis)
Source: World Bank, International Debt Statistics
450
400
350
300
250
200
150
100
50
0
1200
1000
800
600
400
200
0
1970
1972
1974
1976
1978
1980
1982
1984
1986
1988
1990
1992
1994
1996
1998
2000
2002
2004
2006
2008
2010
Argentina
Brazil
Chile
Colombia
Mexico
Peru
Venezuela, RB
*Latin America & Caribbean (developing only)

Some day Latin Amerian countries will learn that they <u>don't</u> grow with foreign savings

- That the best form of coping with the foreign constraint is to manage the exchange rate.
- That foreign savings don't <u>add</u> to domestic savings but usually involve a high rate of substitution of foreign for domestic savings.
- That foreign indebtedness:

 –first, increases consumption rather than invest

 –second, creates financial fragility and dependence.

 –third, leads to financial crises.

Managing the exchange rate involves two things

1. If the country faces the Dutch disease,
to act on the value of the exchange rate to make competitive the business enterprises utilizing technology in the world state of the art, by imposing a tax on exports
2. In any case,
to act on supply and demand of foreign money to limit the fluctuation of the market exchange rate around the exchange rate value, by buying and selling reserves and controlling capital inflows.

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