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Statement of the Shadow Financial Regulatory Committee on International Debt

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United States loans to Latin American debtors are, on average, now worth about fifty cents on the dollar. As a result, additional loans to these countries represent a transfer of United States wealth to foreigners.

Since the international debt problem first came to public attention in the summer of 1982 the principal debtor countries have continued to increase their debt absolutely and relative to exports. The problem of servicing the debt has increased.

Additional lending by the U.S. government, international agencies, or financial institutions to permit countries to service outstanding debt is at best a stopgap measure. A long-term solution to the international problem requires more than additional loans. Policies should be designed to bring the debtor countries to a position at which they can service their debt and borrow in the market without intervention by governments or international agencies. This cannot occur until the debt export ratios and debt service as a percentage of exports fall substantially. In recent years, these ratios have increased.

The debtor countries have three options. First, they can default. Wealth would be transferred from creditors to debtors. Equivalently, creditors can forgive or write off part of the debt. Second, the debtor countries can further reduce their domestic spending by lowering living standards, thereby increasing exports and their ability to service the outstanding debt. This would require a new round of austerity. Third, debtor countries can sell assets. A sale of domestic assets transforms debt into equity, but does not necessarily reduce the long-term servicing costs of the debtor countries.

The Shadow Financial Regulatory Committee offers a four-part program to move toward a long-term solution. First, the U.S. government and international agencies should reduce their lending and their involvement in the debt rescheduling process. Debtors and creditors should be encouraged to develop a long-term program through negotiation without participation of the U.S. government or international agencies.

Second, a main source of capital for debtor countries, particularly Mexico and Argentina, should be the capital that nationals of these countries invested abroad during the 1970s and early 1980s. Debtor countries should adopt policies that would repatriate this capital through voluntary private inflows.

Third, debtor countries should increase productive efficiency and improve resource allocation. A major step in this direction can be achieved by beginning or accelerating the privatization of state industries and parastatal firms.

Fourth, to encourage both repatriation and privatization, countries can exchange dollar denominated debt for (domestically denominated) equity. Exchange of debt for equity should be made at current market prices of the debt. These would reduce foreign investment service obligations if the exchanges occur through a voluntary repatriation of capital by nationals of the debtor countries.

To reduce debt/export ratios, debt must grow more slowly than exports. For countries like Brazil or Mexico, the historic average growth of exports is sufficiently high that debt service requirement as a share of exports and the ratio of debt to exports can be reduced substantially in five to seven years, if debt is held at present levels. Debt equity swaps of $2 to $3 billion per year to offset an equivalent capital outflow would permit the debt to remain constant. Within a decade, at the growth rates of exports of the past ten years, Brazil and Mexico would be close to the point at which they could return to the marketplace. For other large debtors -- Argentina is an example -- a longer time or more extensive program would be required. Additional lending will only impede the necessary adjustments.

It is the Committee's policy that members abstain from participating in the formulation of policy statements in instances in which they have a direct personal or professional involvement in the matter that is the subject of the statement. Accordingly, Mr. Hawke abstained from participating in or voting on this statement.