

Public Debt: Who owns who? by Gabriel Strautman¹

The recent announcement of Brazil's upgrade to the net external creditor position – when a country's external assets surpass its liabilities – was very welcome by the Brazilian Government's financial authorities as a triumph of our economic policy. According to the government, for the first time and thanks to the high level of our international reserves, we have sufficient resources to pay off the external public and private debt if we wished to do so. That joy, however, is justified only from a strictly political perspective, since from a financial point of view the external debt is today a minor problem, compared to the internal debt, and the payment of both still represents an obstacle to progress on pressing social needs for the country.

According to the Central Bank, in January 2008, Brazil's total external debt (both public and private) was US\$ 196.2 billion, against assets amounting to US\$ 203.193 billion over the same period. This means that, in January, Brazil had a negative external debt of US\$ 6.893 billion, which led the country to reach a net external creditor position.

Brazilian external assets are mainly made up of the country's International reserves – which in January amounted to a record US\$ 187.534 billion – not counting the US\$ 12.864 billion in commercial bank assets and the US\$ 2.819 billion in foreign credits. As regards (passive) external debt amounts it is interesting to point out that as from March 2001 the Central Bank excludes from calculations the value of intercompany loans (debts of multinational subsidiaries established in Brazil with parent companies abroad). By adding these loans' worth – which in December 2003-February 2008 soared from US\$ 20.484 billion to US\$ 49.926 billion – Brazilian total external debt surpasses US\$ 240 billion, an amount which exceeds total assets and contradicts the so-called net external creditor position.

But even without taking intercompany loans into account and accepting the net external creditor position, we are still far from considering the debt issue as problem solved. Evidence of that is the fact that Central Bank estimates for 2008 nominal deficit – final national accounts after debt service – is 1.6 points of GDP. A great part of the national budget continues to be allocated to the repayments and service of the external and internal debts, which represent 30.59%² of the general budget of the Union³ implemented in 2007⁴. In order to have a notion of proportions, in the same year only 5.17% of budget resources were spent on health, 2.58% on education and 0.41% on science and technology.

In spite of financial expenditure regarding the external and internal debts virtually taking in one third of the federal budget, as has just been pointed out, and despite these items being the ones that have grown the most over the last years, they are rarely considered in debates on the necessity to increase public spending efficiency. This observation was made by Ronaldo Coutinho Garcia, of the Applied Economics Research Institute (IPEA),

¹ An economist of the Institute of Alternative Policies for the Southern Cone (PACS), member of the Brazilian Network on Multilateral Financial Institutions and of the Jubilee South Network.

² If taken into account the rescheduling payments (repayments with debt financing), the percentage increases to 53.2% of the budget implemented in 2007.

³ Reference to the Brazilian national budget (TN).

⁴ Figures taken from the third edition of "ABC da Dívida", available at <http://www.divida-auditoriacidada.org.br/>

for whom, curiously, debts service, commissions and repayments are “untouchable, unpronounceable, nonexistent for fiscal policy, even if they are a heavy burden”⁵.

According to Garcia, the current structure of public spending favours a limited number of families and economic groups with access to the financial market, to the detriment of the majority of Brazilians, who depend on the development of redistributive public policies. Thus, the fact of not acknowledging the payment of public debt service equals to acknowledging the “untouchability of these privileges”, when the untouchable should be the guarantee of the social and individual rights of the majority.

The opposition to external debt payment became the banner of struggle of Latin American social movements and leftist parties after the indebtedness process launched by military governments in the 1970s, and the subsequent debt crisis in the 1980s, brought about by a unilateral increase in US interests, which ruined indebted countries’ finances. Throughout this whole period, the activities of multilateral financial institutions, such as the World Bank and the International Monetary Fund (IMF) have been decisive. Whereas the first promoted the indebtedness of peripheral countries in the 1970s, offering easy credit for large infrastructure projects – many of which were questionable – the second was responsible for the imposition of major market liberalization policies in indebted countries, as a condition for access to loans during the 1980s crises. These institutions’ degree of commitment to international capital interest made them turn into targets of the leftist movements’ struggle as well.

By announcing Brazil’s new net external creditor position, thus suggesting that the debt problem has been solved, the government seeks a political victory, repeating a strategy also used in 2005, when we cancelled our debt with the IMF through a US\$ 15.5 billion early payment. For this reason, our debt cancellation with the IMF as well as the so-called external debt overcoming do not have the same meaning in the current political and economic circumstances. The IMF is currently attempting to overcome a legitimacy crisis arisen after the evident political failure of liberal reforms imposed on countries by the institution throughout the 1990s⁶. Notwithstanding the fact that the problem is far from being solved, as it has been already seen through the analysis of the gap in public funds. Although the external debt appears to be a minor problem, since we have an internal debt at least three times as large.

In February 2008, the internal debt reached the astronomical figure of 1.242 trillion reais, which amounts to nearly three times the external debt value estimated in 417 billion reais⁷. If we consider the Central Bank’s open market operations (OMO), that is to say, the placing of securities in the market aiming at the liquidity mainly generated by dollars purchase, the internal debt surpasses 1.4 trillion reais⁸. Of the 237 billion reais earmarked from the federal Budget to Brazilian public debt payments and service in 2007, 219 billion were allocated to internal debt payment, against 18 billion allocated to the external debt, which means 12 times as much.

⁵ Garcia, R. G. “Despesas correntes da união: visões, omissões e opções”. Brasília: Ipea, jan. 2008 (Paper for discussion nº 1319)

⁶ It is odd to see how despite debt cancellation with the IMF, which frees us from the conditionalities imposed by this institution, we continue faithfully abiding by the same orthodox economic policies of the past. The best example of that is the effort to generate huge fiscal surpluses, which produce the resources for debt payment.

⁷ This figure was turned into reais for the purposes of its comparison with the external debt. This figure includes intercompany loans.

⁸ <http://www.bcb.gov.br/htms/infcon/demab/ma200802/index.asp> (table 11)

A meteoric expansion of the Brazilian internal debt, closely related to the external debt which led the country to the 1980s crisis, which was multiplied by seven over a decade. After the Real Plan implantation in 1994, the increase in imports following the immediate appreciation of the Real resulted in the country's trade balance deficit. This imbalance had to be made up for by attracting hot money, which came into the country for the purposes of making a profit through one of the highest interest rates worldwide. One of the ways out suggested by Brazilian economic policy agents was turning the public debt – resulting from the intense external indebtedness process in previous decades – into securities negotiable in the financial market⁹. Thus, many of the external creditors became “internal”, a process which is increasingly intensifying the more acute the recent valorization trend of the Real against the Dollar¹⁰ becomes.

Between 1978 and 2007, our external debt which was US\$ 52.8 billion soared to US\$ 243 billion. In the same period, we paid US\$ 262 billion more than what we borrowed. Therefore, the relation between the current internal debt and the debt generated over the years of dictatorship and restructured many times during the democratic period means we continue paying for an illegitimate debt that has been already paid up.

If we consider, additionally, the incalculable environmental liabilities resulting from major projects financed with debt resources, we will come to the conclusion that we are the true creditors of that debt.

We should, therefore, abide by the 1988 Federal Constitution which, in its 26th article, in the transitory provisions section, determines the carrying out of an external debt audit, which would open an opportunity to restart the debate over the burden of debt service on the budget. And that is exactly what the Ecuadoran Government is doing, led by President Rafael Correa, who in 2007 set up an Integral Public Credit Audit Commission (CAIC) under the responsibility of the country's Ministry of Finance, with an aim to analyse and assess the indebtedness process in 1976-2006¹¹.

The work develops in order to give a detailed account – not only to evidence the economic and financial impacts, but also to reveal the environmental impacts derived from the indebtedness process. This means the auditing will aim at identifying interest rates, commissions and penalties imposed, often in an unilateral manner in credit agreements – thus violating the sovereignty of borrowing countries – as well as the consequences of the conditionalities assumed in loan agreements regarding the population's living conditions. Thus, the relation between the goal of a financed project and the social and ecological impacts resulting from same will be analysed, from a multidisciplinary perspective and with a broad approach, which help to prove and make visible the claimed debt's illegal and illegitimate character.

⁹ Fattorelli, M.L. and Ávila R. “A dívida e as privatizações”. Available at <http://www.divida-auditoriada.org.br/artigos/artigo.2007-05-18.8663125666>

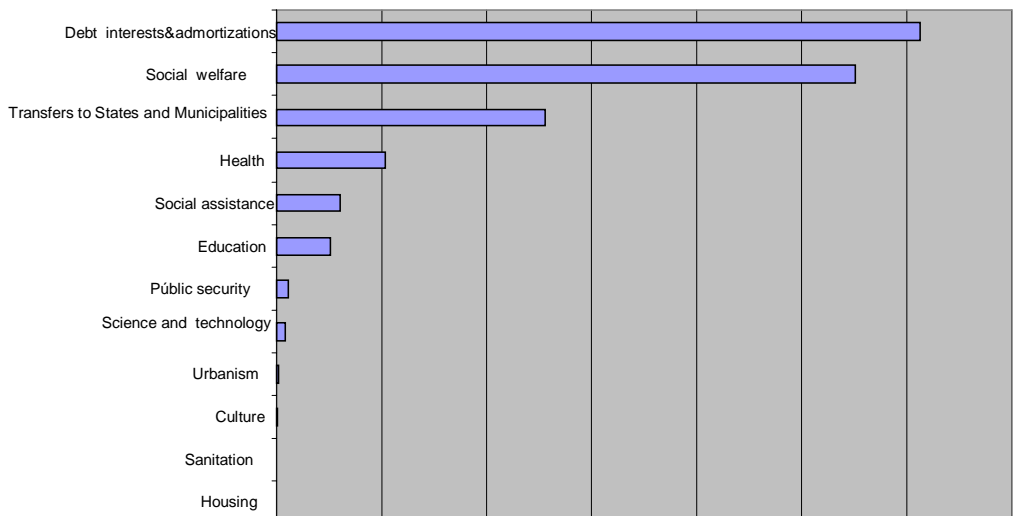
¹⁰ “In 2007, the value of the Real rose 20% against the dollar. Therefore, the foreign investor who brought dollars in the beginning of 2007 in order to invest in Brazilian internal debt instruments made an average 13% profit in interest, plus 20% when they changed their profits into dollars. Subsequently, in 2007, foreigners gained an actual interest rate (in dollars) amounting to over 30% annually”. Ávila R. “A dívida não acabou”. Available at www.divida-auditoriada.org.br.

¹¹ “Auditoria Já!” Nº 0, available at <http://www.jubileubrasil.org.br/>

We observe with great expectation the developments in the Ecuadoran auditing process, with the hope of following its example in the near future. We expect the strength of its results will pave the way for restarting the debate over the debt burden on the Brazilian society, and that we may, in a wider perspective, change the current perception by proving that nations are the true creditors of that debt.

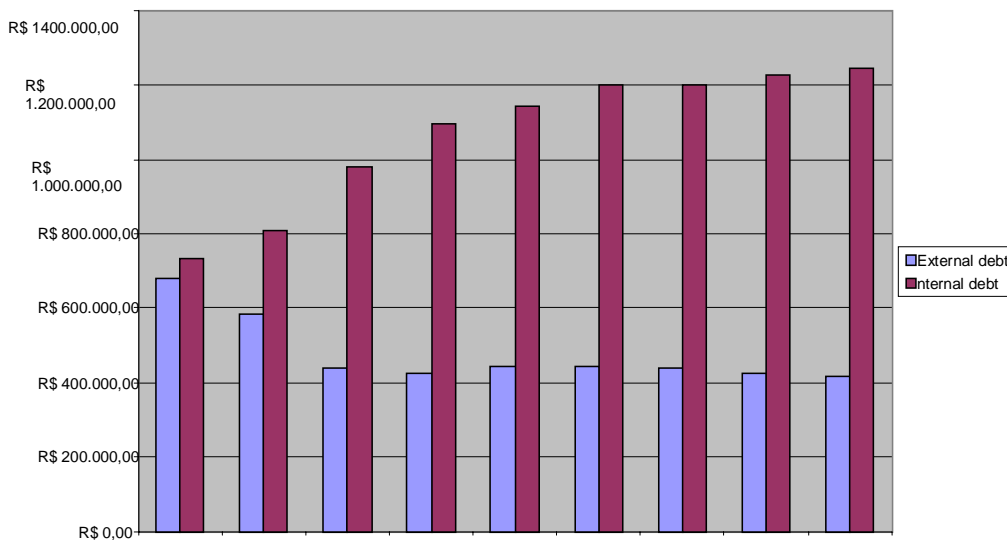
The following charts offer an account of the Brazilian debt burden compared to other Budget items.

Brazil: Items on the Union's General Budget Executed until Dec 31, 2007 (%)



Source: Auditoria Cidadã da Dívida

Brazil: Evolution of External/Internal Debts (R\$ millions)



Source Central Bank