

Brazil's new 'cruzado plan': how to do nothing about debt

by Mark Sonnenblick

The "Cruzado Plan" unveiled by Brazilian President José Sarney Feb. 28 is one of the most flamboyant exercise yet for *not* dealing with the debt crisis. While throwing the brakes on an inflationary spiral, it does nothing to deal with the real causes of Brazil's hyperinflation.

Under the plan, Brazil joins Argentina in applying what economists call "heterodox shock" to outlaw inflation. Wages are frozen for a year and prices are frozen indefinitely. As with the Argentine Austral Plan, a new "inflation-proof" currency was born and its relationship to the dollar fixed.

The wonder of the plan is that it gives hope of ending inflation, which has been over 200% for the past two years and whose February rate of 14.36% gave every promise of an annual rate soaring over 300%. The Cruzado Plan differs, at least on the surface, from orthodox economic shock as applied in Germany by Hitler's economics minister, Hjalmar Schacht, or in Pinochet's Chile, and Shimon Peres's Israel by the academic children of Milton Friedman. In these cases, police repression had to be applied against workers whose wages were cut from the beginning. In Brazil, most wages were raised at the onset of the program, while prices were frozen.

Psychological warfare

All Brazil stopped working at 9:30 a.m. on Friday February 28 morning so all could hear the announcement of a surprise economic package. Film clips of President Sarney meeting the day before with top military leaders were flashed repeatedly on the screen. Then Sarney told his countrymen, "Today is the beginning of a life-and-death war against inflation." He quickly passed the microphone over to Finance Minister Dilson Funaro, who explained how the new program is to work.

At first, people were perplexed and confused, our Rio Bureau reports. Brazilians had learned to live with what for most others would be unimaginable inflation. Everything in the economy was indexed, rising roughly in tandem with inflation itself. Interest rates and other financial factors were totally protected from growing inflation, while wages, which caught up with inflation only every six months, were seriously eroded.

Sarney's wage-price freeze brought more popular euphoria than when he proclaimed a "New Republic" at his

April inauguration as the first civilian president in two decades. Political commentators said the "New Republic" only started Feb. 28. Knowing full well that the government's price-control board, SUBAN, could never enforce fixed prices over a land area larger than the continental United States, Sarney implored consumers to take responsibility for enforcing the measure.

They hardly needed to be asked. When a dozen stores tried to raise their prices immediately after the Sarney speech, angry customers ripped them apart. Hours later, Federal Police Chief Romeu Tuma, long known for his highly centralized law-enforcement practices, went on television to encourage citizen arrests of price hikers.

Consumers armed with official price lists patrolled store aisles. Two prestigious members of the National Monetary Council were caught having ordered their store employees to spend the night before Sarney's speech marking up prices, and were fined. Following over 10,000 consumer complaints and dozens of highly publicized arrests, the price freeze was made to stick, at least in the beginning.

The consumer enforcement orgy, a virtual second Carnival, was part of the "psychological" aspect of the Cruzado Plan, which its drafters consider more important than any other aspect. Such a novel de-indexation plan was formulated in studies commissioned in 1984 by International Monetary Fund director Alexandre Kafka. This shadowy Czech-born economist with Brazilian nationality sits out of sight in Washington running the economic policies of most Third World countries like a master puppeteer.

Kafka's original plan was for Tancredo Neves, the father-figure who was supposed to be the first civilian President, to use his immense popularity to impose shock austerity policies with the new psychological packaging shortly after his April 15, 1984 inauguration. But Neves died before being sworn in, and Sarney was thrust into the presidency with the image of a graceless hatchet man who had forced the Senate to rubber stamp unpopular measures for the military dictatorship.

To build credibility, Sarney made nationalist speeches against the IMF and reflat the economy by means of running the "printing press" for yet more credit and subsidies to the nation's exporters, and for small increases in real wages. As a result, the GNP grew by 7%, recuperating a small part

of what it had lost during the previous three years of depression.

Dilson Funaro, who became finance minister in September, emerged as the champion of Brazil's recovery. Funaro has taken a hard line against the IMF in public and is committed to maintaining 5-6% growth this year. He has concentrated economic policy control in his hands, even more than Delfim Netto, Brazil's "economic czar" from 1979-85, had done. The difference is that Funaro, a not-so-successful Sao Paulo toy manufacturer, is a "nice guy" and knows how to make friends in democratic society.

Even more than Delfim, for whom winning over a handful of backroom authoritarians was all that was required, Funaro is a master at "packaging" economic policy. It also seems that he shares Delfim's very Brazilian character of being a pragmatist, of utilizing higher principles like "sovereignty" and "justice" as rhetoric for the end of winning some mundane advantage.

Thus, Funaro proclaimed with great aplomb on the morning of Feb. 28, "Brazil will never again sign agreements with the IMF which allow Fund economists to come here and determine our economic policies." Three days later, the *New York Times* quoted him confiding, "I'm carrying out a very tough policy, much tougher than if I went to the IMF. And I'm achieving, because I don't have the IMF behind me. My Congress would not approve policies imposed by the Fund. . . ."

Rather than being scandalized, Brazilians tend to admire someone with *jeitinho*, a person who pulls off a clever hustle, even at their own expense.

Sarney and Funaro embarked on the Cruzado Plan for primarily political reasons. People were getting bored with the government. On Feb. 25, the largest element of the governing coalition, the old PMDB party of opposition to the military government, announced it was going its own way. The left end of the party was already in alliance with Rio socialist Leonel Brizola. And many former supporters of the military regime from the Sarney side of the coalition, were making deals with Sao Paulo populist Mayor Janio Quadros, who is anxious to return to the presidency as a right-wing authoritarian.

So, Sarney chose to prove his leadership with a crusade against inflation, which the media had projected as Brazil's crucial problem. The pundits say that if he succeeds, his group will sweep the Nov. 15 elections for governors and a constituent assembly. If he fails, he will blame it on Funaro in an effort to prevent Brizola and Quadros from shortening his term.

Bankers rejoice

During the days before the Cruzado Plan, Brazil's foreign creditors forced the issue by suddenly canceling \$71 million of the \$15.5 billion in short-term credit lines which keep Brazil solvent. Within 48 hours after Brazil "bit the bullet," Funaro was rewarded. Not only was the full \$15.5 billion

guaranteed for another year, but interest rates were reduced on an equal amount of principal due in 1985 and 1986.

Funaro got a gift. Brazil would receive interest rate cuts of 7/8 of one percent on \$15.5 billion of its \$104 billion debt. Finally, Brazil would be paying the same rate as Mexico. It was a good start, though not Funaro's ultimate ambition, which he had expressed Feb. 26: "I expect within the next months to use Mexico's fight with the bankers over interest rates like a judo fighter, to win better rates than Mexico."

So much for the solidarity among debtors which the Cartagena Group proclaimed at its Punta del Este meeting on Feb. 28! Funaro, of course, did not go to the meeting. Brazil has "astutely" played off the hardships of others, but has consistently thwarted efforts to unite debtors to reform the world financial system so that real investment and growth could take place.

How much was Brazil rewarded for fighting against both inflation and debtor unity? Funaro himself gave the figure of \$150 million. That is, just over 1% of the \$11 billion Brazil will pay in interest this year.

Further interest relief is dependent not on inflation statistics, which bankers really could care less about. The critical question is whether Brazil continues to divest ownership of such strategic industries as the state oil company, Petrobras, and the state mineral company, Vale do Rio Doce.

The banks that Henry Kissinger represents demand their debtors cut "inflation," because "shock therapy" gimmicks generally end up handing a country's natural-resource and industrial base over to foreign interests. The Brazilian government has been milking the state-run productive sector so much that companies have to sell off assets in order to fund priority projects. As a prelude to the Cruzado Plan, it increased tax collections by 10% in real terms last fall. Any "anti-inflation" move which implies further budget cuts or tighter credit, will cause further divestment, and further domestic recession.

The real cause of Brazil's inflation is the incredible cost borne by the domestic economy so that Brazil could export double what it imports and use the \$12-13 billion trade surplus to keep current on debt interest payments. There are a myriad of these costs. The Brazilian government wastes the equivalent of \$2 billion per year in subsidizing alcohol production (see page 9) to achieve marginal foreign exchange savings. Brazilian steel sells cheaper in Baltimore than in Sao Paulo, thanks to generous export subsidies, fuel discounts, tax rebates, bounties, and losses taken by producers on export sales. The population pays in a myriad of ways, which boil down to radical cuts in consumption levels. When the government briefly let consumption recover a bit at the end of last year, without allowing imports to increase, inflation started to mount.

So long as Brazil continues to sabotage debtor unity, it is doing nothing but wearing out its population and its productive apparatus, if not giving it away to creditors to pay unpayable debts.