

The country-Risk, spoliation and submission

Introduction

For years, Brazil has adopted neo-liberal economic and monetary policies, aiming to conquer the credibility of the markets and financial agents. One of the instruments that surveys this “credibility” is the “country-risk”, calculated by JP Morgan bank and several international agencies. This risk is associated with the country capacity to pay its external debt – private and public - and to assure the free exit of the foreign capitals.

Although the country-risk is usually presented as an objective index, its calculation is subjective. This subjectivity involves another factors beyond the capacity of the countries pay debts, as the interests defended by the institutions that calculate this “risk”. On January 2004, the Morgan Stanley agency was condemned, due to the divulgation of a unfavorable report about the LVMH company, the biggest company of luxury articles in the world. As proven, the Stanley was helping directly the Gucci company, rival of the LVMH (see the box below).

Although the conduction of the economic policy in our country has always corresponded to the requirements of the IMF and the “financial markets”, and this “default-risk” never had materialised during all these years, the country paid much, very much due to the calculations created by these institutions. However, although our high social and economic sacrifice, we didn't question these institutions about the financial damages they had caused to our public accounts, and the moral damage caused by the unfavorable avaluations.

This work aim to spread ideas to allow countries to be free of the restrictions imposed by the agencies in the process of risk evaluation. And, why not, to advance in the elaboration of reparation actions, as in the case of LVMH.

What`s the “country-risk”?

The country-risk is measured by the additional parcel of interests a country pay in comparison with the North American Treasure, in a operation with the same value and payment conditions. The creditors say that these additional interests are necessary to compensate the risk of default of the developing countries. According to this “rule”, the risk increase if the government policies are unfavorable to the creditors.

The value of this “risk” is presented in the opening of the main TV reporters with so importance that we think that all the domestic economy, in the immense majority of the homes of the country, is applied in Brazilian bonds that circulate in the international market. The truth is different. The massive information about the performance of the stock markets and the values of the bonds and the country-risk demonstrates the power of the financial aspect of economy, and how the media show these information as the most important for the people. This financial economy, showed by the me-

Jornal do Brasil, January 13, 2004

Morgan Stanley is condemned

PARIS – Yesterday, the American bank Morgan Stanley was condemned to pay a 30 million euros (about USS 38 million) indemnity to the LVMH, the biggest company of luxury products in the world, controller of marks as Louis Vuitton and Mōet & Chandom. Stanley produced a harmful report about LVMH. The sentence of judge Gilbert Costes, of the Paris Commerce Court, was considered “totally wrong” by the bank, that affirmed that will appeal of the decision.

In the Costes` judgment, the Morgan Stanley committed serious crime against LVMH, causing moral and material damage to the company image. The report, produced by Claire Kent, the most respected analyst for the sector, affirmed that the quotes of the group were superevaluated and was divulged that the bank helped the Gucci - rival of LVMH - to reject purchase offers of the LVMH.

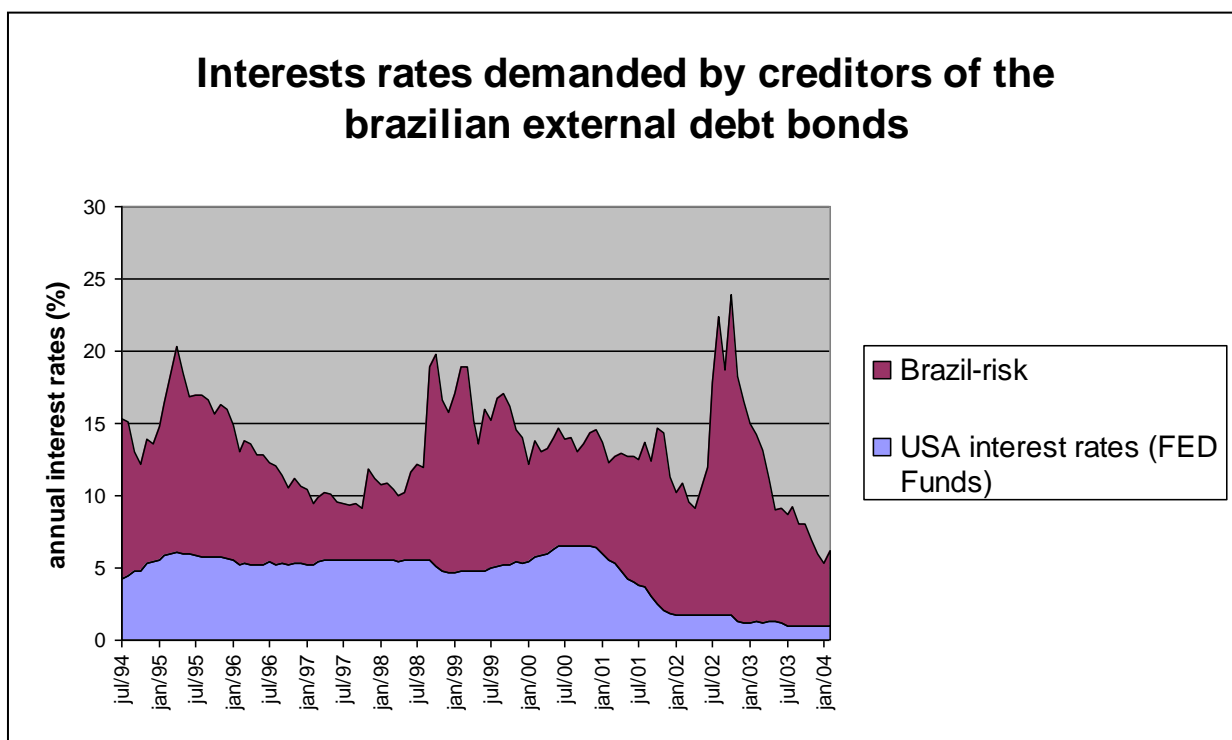
Bloomberg and EFE agencies

dia, isn't the economy of the job, the production, the income, the "real economy". The media spread the information of the speculation economy, the financial profits.

These notices are divulged by the media aiming to make people judge its government in accord to the fall of the country-risk and the ascent of the stock markets, and not in accord to the increase of the unemployment or the fall of the Gross Domestic Product (GDP). These informations are divulged by the media aiming to make people do not perceive how the total freedom for the goods and capital circulation caused the increase of the social inequality, the worsening of the quality of the jobs, the hunger and the misery. This is done to submit governments and society to the interests of the big financial capital.

The country-risk calculation is presented as an objective analysis, depending on the perception of the financial market about the difficulties of the country to pay its international commitments, not only its debt, but also the another ones that derive from any foreign investments. However, this evaluation is more complex and involves another factors.

In fact, all year, the interests imposed to Brazil by creditors are very bigger than the interests demanded by these same creditors to the US government. In the graph below, it is verified that the component-risk is responsible for the main part of the interest rates demanded by the creditors.

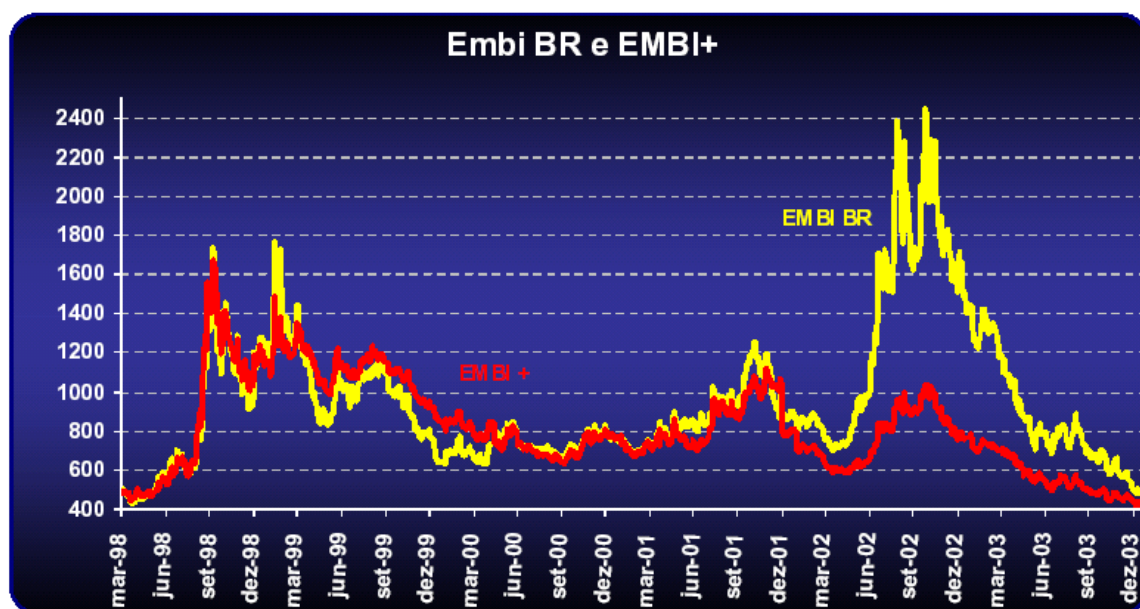


Source: FED and JP Morgan

But the oscillation of the risk can't be explained by this "fear" of the creditors. Although money is a special merchandise, it's also influenced by events of offer or demand excess. In 2002, for example, the investors, still under the influence of the frauds in the stock markets in U.S.A. and Europe, had retracted its remittances to the development countries. This credit contraction and this aversion to the risk raised the interests paid by all borrowers, independently of its objective conditions or how they were perceived by the owners of the money. In contrary direction, in 2003, the low interests practised by the developed countries, many times incapable to cover only the depreciation of the currency, increased substantially the availability of credits and, as a miracle, the risks of several countries had fallen, not only in Brazil, but also in countries that had recently suspended payments of its debts, as Mexico, Korea, Thailand, Indonesia, Russia and Uruguay. Even the risk of Argentina, in moratorium, fell. We have below a graph that shows this evolution. The red line ("Embi+") means

the risk of the emergent countries, calculated by JP Morgan Bank, from the average of the risks of diverse countries, weighed in accordance with its participation in the international bond market. We also have below a table that shows the significant reduction, in 2003, of all country-risks that compose the calculation of the Embi+, by JP Morgan bank.

Brazil-risk and developing countries risk



This graph was obtained from the “Monthly Report of the Country-risk”, of Global Invest, december/2003. Note: in this graph, the risk is measured by basis-points, that mean the annual interests multiplied 100 times. For example: a risk of 500 means that the country must pay an annual interest rate 5% above the interest rate paid by US.

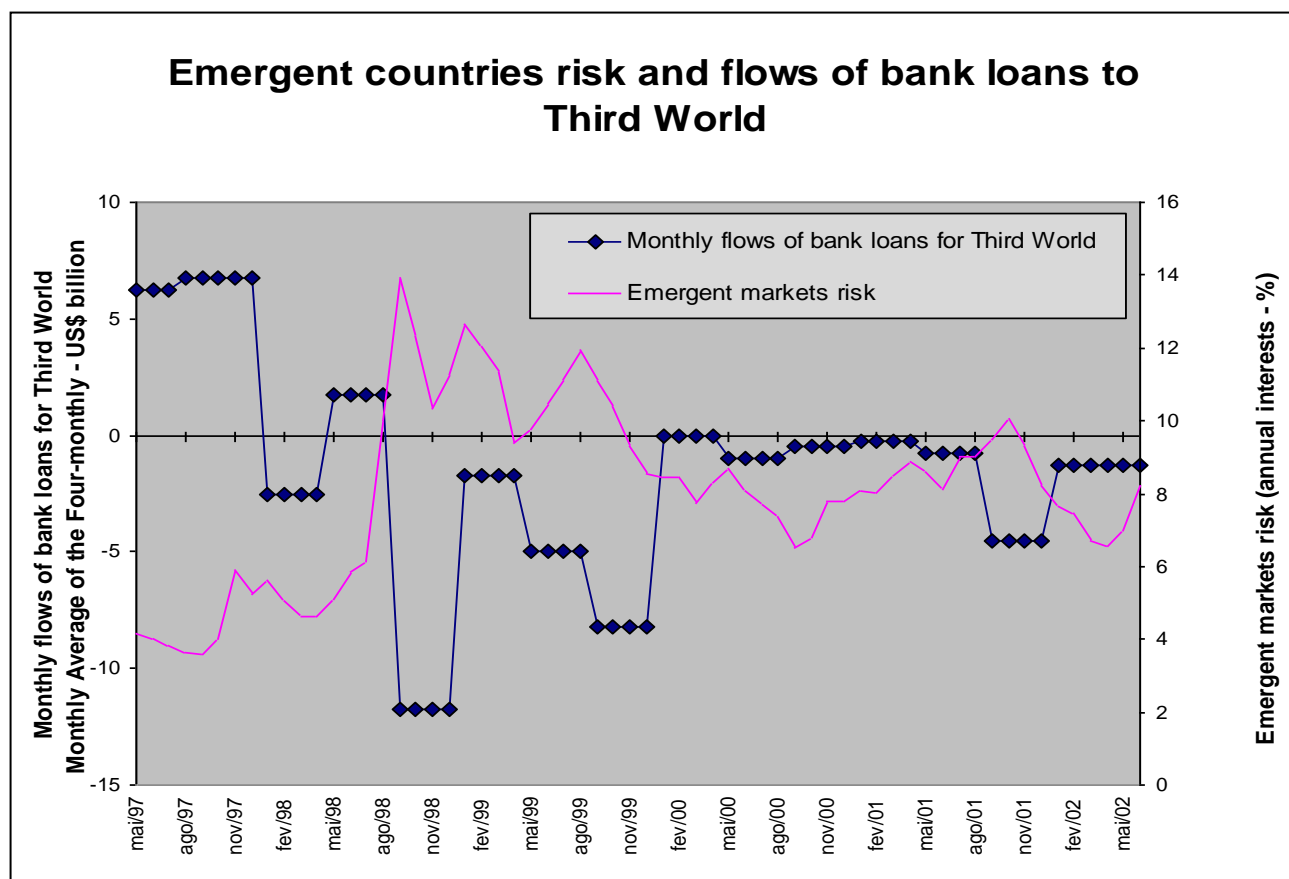
Table 1 - Variation (%) of the country-risk in 2003, in basis-points

Annual variation of the Country Risk			
Country	Risk on Jan 2003	Risk on Dez 2003	Var. in the year
1 Brasil	1438	463	-67,8%
2 Nigéria	2215	733	-66,9%
3 Egito	383	138	-64,0%
4 Ucrânia	668	258	-61,4%
5 Polônia	178	69	-61,2%
6 Marrocos	390	160	-59,0%
7 Malásia	166	71	-57,2%
8 Equador	1796	799	-55,5%
9 Turquia	687	309	-55,0%
10 Peru	606	312	-48,5%
11 Venezuela	1119	593	-47,0%
12 Rússia	472	257	-45,6%
13 EMBI +	759	418	-44,9%
14 África do Sul	233	142	-39,1%

15 México	324	199	-38,6%
16 Bulgária	288	177	-38,5%
17 Colômbia	640	431	-32,7%
18 Panamá	439	335	-23,7%
19 Filipinas	524	415	-20,8%
20 Argentina	6355	5739	-9,7%

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It's verified that the oscillation of the country-risk is explained by the disposal of the creditors to move their capitals to the Third World countries, and not by the execution of determined politics by governments of the debtor countries. The graph below shows this correlation clearly. It compares the index of the emergent countries risk with the flow of capitals for these countries. We verified that the capital flow has an exactly inverse relation with the risk.



Source: BIS and JP Morgan

Then, we can prove the inverse correlation between the risk stipulated for the emergent countries and the capital flows for these countries. When the countries presented a risk under 6% (until middle 1998), there was a positive flow of resources. Since then, the flow is negative. The events occurred on April 2004 are also important, when the simple threat of the rise of the US interest rate (that would reduce the offer of resources to the emergent countries) induced JP Morgan, Citigroup and Merrill Lynch agencies to reduce the classification of the Brazilian bonds.

Therefore, we can say that the risk has a bigger correlation with the events of the international conjuncture than with specific policies of each country.

The requirement of the risk payment is not supported by norms of international law and also does not obey a logic or a mathematical coherence, because all the commitments have been fulfilled religiously by Brazil. Our country is one of the best remunerative of the foreign capital during all these years. This “risk”, determined by JP Morgan and some international agencies, is an artificial creation and serves to the collection of this additional interests. If this “risk” never was implemented, why we continue to pay this additional? In the truth, this has been an onerous mechanism that contributes for the uncontrolled growth of the external debt.

How much is the “risk” burden?

The worsening in the terms of payment of the countries incorrectly evaluated by the international agencies is visible. If we compare the terms of payment of the Brazilian external debt with the US one, we will see that this last one is much more easily quit than the Brazilian. The tables below simulate the payment of an US\$ 100 hypothetical debt by Brazil, with an interest rate of 12% per year, and by U.S., with interests of 1% a.a.. We see that, in the Brazilian case (Table 2), there will be necessary 20 semester installments of US\$ 5 for the payment of the debt, and more US\$ 68,7 of interests, paid in 10 years.

Table 2. Payment of an US\$ 100 hypothetical debt by Brazil (with interests of 12% per year)

SEMESTER	DEBT SUM	SEMESTER INTERESTS (6%)	INTERESTS PAYMENT	DEBT PAYMENT
0	100			-
1	100	6	6	5
2	95	6	6	5
3	90	5.7	5.7	5
4	85	5.4	5.4	5
5	80	5.1	5.1	5
6	75	4.8	4.8	5
7	70	4.5	4.5	5
8	65	4.2	4.2	5
9	60	3.9	3.9	5
10	55	3.6	3.6	5
11	50	3.3	3.3	5
12	45	3	3	5
13	40	2.7	2.7	5
14	35	2.4	2.4	5
15	30	2.1	2.1	5
16	25	1.8	1.8	5
17	20	1.5	1.5	5
18	15	1.2	1.2	5
19	10	0.9	0.9	5
20	5	0.6	0.6	5
FINAL DEBT	0	0	-	-
PAYMENTS SUM			68.7	100

In the American case (Table 3), there will be necessary the same 20 installments of US\$ 5 for the debt payment, but it will only be necessary US\$ 5,725 of interest payments.

Table 3. Payment of an US\$ 100 hypothetical debt by USA (with interests of 1% per year)

SEMESTER	DEBT SUM	SEMESTER INTERESTS (0,5%)	INTERESTS PAYMENT	DEBT PAYMENT
0	100	-	-	-
1	100	0,50	0,50	5
2	95	0,50	0,50	5
3	90	0,48	0,48	5
4	85	0,45	0,45	5
5	80	0,43	0,43	5
6	75	0,40	0,40	5
7	70	0,38	0,38	5
8	65	0,35	0,35	5
9	60	0,33	0,33	5
10	55	0,30	0,30	5
11	50	0,28	0,28	5
12	45	0,25	0,25	5
13	40	0,23	0,23	5
14	35	0,20	0,20	5
15	30	0,18	0,18	5
16	25	0,15	0,15	5
17	20	0,13	0,13	5
18	15	0,10	0,10	5
19	10	0,08	0,08	5
20	5	0,05	0,05	5
FINAL DEBT	0	0,00	-	-
PAYMENTS SUM			5,725	100

If USA had destined the same annual amount of resources that Brazil did to pay its debt, with a interest rate of 1% per year, we see, in Table 4, that the american debt would be totally payed in only 12 semesters, and not 20, as in the Brazilian case. In the end of the 20 installments, the Americans already had payed US\$ 60,78 more than they had to pay.

Table 4. Payment of the US debt (with interests of 1% per year) with the resources spent by Brazil

SEMESTER	DEBT SUM	SEMESTER INTERESTS (0,5%)	INTERESTS AND DEBT PAYMENT
0	100,00	-	-
1	100,00	0,50	11,00
2	89,50	0,50	11,00
3	79,00	0,45	10,70
4	68,75	0,40	10,40
5	58,74	0,34	10,10
6	48,99	0,29	9,80
7	39,48	0,24	9,50
8	30,22	0,20	9,20
9	21,22	0,15	8,90
10	12,47	0,11	8,60
11	3,98	0,06	8,30
12	-4,26	0,02	8,00
13	-12,24	-0,02	7,70
14	-19,96	-0,06	7,40
15	-27,42	-0,10	7,10
16	-34,62	-0,14	6,80
17	-41,56	-0,17	6,50
18	-48,23	-0,21	6,20
19	-54,64	-0,24	5,90
20	-60,78	-0,27	5,60

The “risk” does not affect us only in the financial aspect. The country-Risk functions, also, as a blackmail to the governments, forcing them to adopt adequate politics to the creditors. The first graph of this text indicated a big rise of “Brazil-risk” in the pre-electoral period, on the 2th semester of 2002, when the leftist candidate to the presidency, Lula, had rise in the electoral polls. To influence the behavior of this favourite candidate, the “market” started to demand high interest rates to buy our debt bonds. Thus, in June 25, 2002, when the country-risk already reached very high levels, Lula divulges the called “Letter to the Brazilian People”, in which it said:

“We will preserve the primary surplus how much it will be necessary to hinder that the internal debt increases and destroys the confidence in the capacity of the government honor its commitments.”

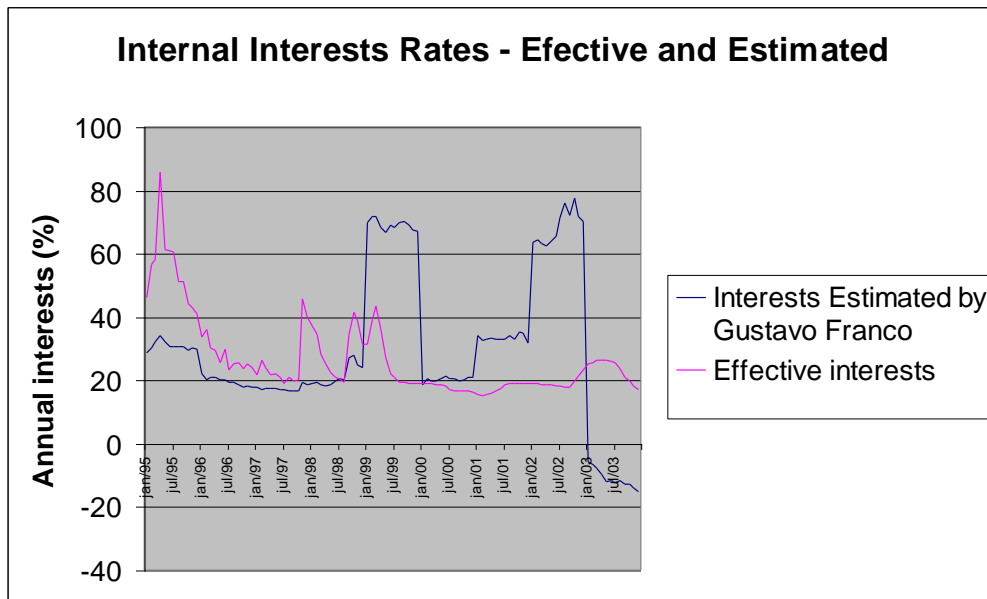
Despite this, the country-risk continued to go up, only lowering in november, after the elections.

If this candidate, when elected and becoming president, continued fulfilling the same economic policy, in a more orthodox form, with higher primary surpluses and more generous remuneration to the investors, that risk evaluation was configured totally wrong. However, it provoked several consequences to the Country, that had its debt increased, difficulties to offer its bonds in the financial market, and was pushed for the onerous agreement with the IMF (september/2002). This agreement ruled the economic policies, with the Pension Reform, Tax Reform, Bankruptcies Law, Independence of the Central Bank... Brazil had to pay all these costs. And the agencies, that made an evaluation mistake?

Box: The internal interest rates: why so high?

In the internal debt, Brazil had always practised one of the biggest interests rates of the world, to attract the foreign capital. According to Gustavo Franco, former-president of the Brazilian Central Bank - who implemented the neo-liberal policy in the Cardoso`s government - the brazilian internal interests would have to be the sum of the FED interests rates, the “Brazil-risk”, and the depreciation of the Real (the brazilian currency), preventing that these investors preferred to destine its money to other countries.

However, if we observe the graph below, we will verify that Franco`s theory doesn`t correspond to the truth. The red line represents the interests effectively determined by the brazilian Central Bank, while the blue line represents the Franco`s sum of the country-risk, annual Real depreciation and US interests. In the period of 1995-1998, the brazilian interest rate was very bigger than the Franco`s estimate.



Source: Brazilian Central Bank, FED and JP Morgan

On the Financial Crises of Mexico (1994/95), Asia (1997) and Russia (1998), the Brazilian interest rate was increased to levels don't explained by any theory. Why Central Bank raised the interests to those levels, that produced our not-payable public debt?

In 1998, creditors already had a big amount of bonds readjusted by US dollar. The previsible strong Real depreciation – that occurred in the beginning of 1999 – made government to offer this kind of bonds in 1998, to eliminate the risk of the foreign capitals. Therefore, in the period of 1999-2002, despite the internal interest rates had been smaller than the Franco's projected interests rates, the effectively paid interests had been much bigger than the graph shows.

In 2003, we had, again, excessively high interest rates, due to the valuation of the national currency. So, if the Franco's explanation was correct, we must have practised negative interest rates (as the graph indicates). However, Brazilian Central Bank continued determining one of the higher interest rates in the world.

But, after all, why our interest rates are so high? In the last years, the politics of interests has functioned to several goals, as the fulfilment of the inflationary goals, the attraction of the external capital and the generation of trade surpluses through the recession, that reduces our imports and deviates the internal production for the exportations. So, the interest rate remains high.

In the case of the inflationary goals, the high of the interests reduces the inflation through the reduction of the economic activity and, therefore, the income of the workers. However, the rise of the interest rates doesn't function to control the prices managed by government, and has a very little effect to control the prices formed in oligopoly conditions, that go up much more than the general inflation average.

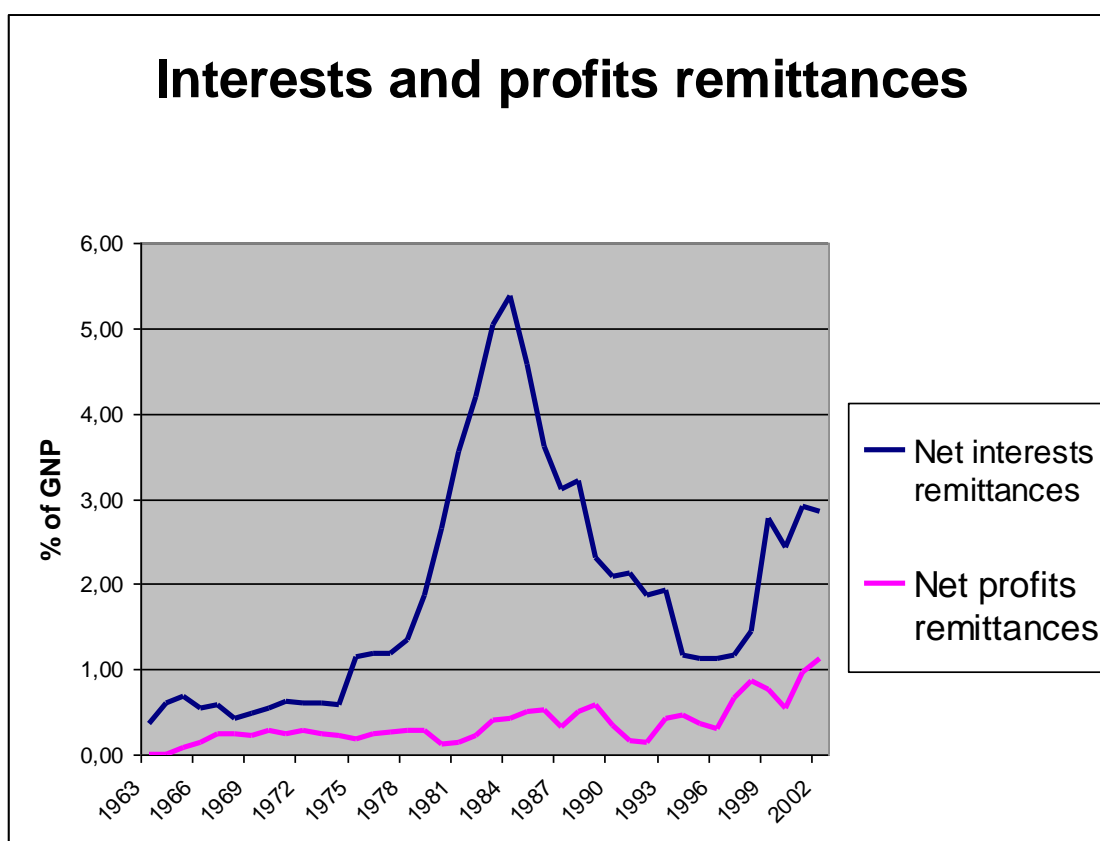
According to DIEESE (Brazilian Inter-Union Department of Social and Economic Studies), the inflation accumulated in 8 years of Real Plan (Jul/94 - Jun/2002) was 126%. However, prices determined in oligopoly conditions had risen 215.1% in the same period. The prices managed by government (mainly public services prices) had risen 238.1%, almost 2 times bigger than the general average of inflation! A study concluded in 2002, from exactly the Brazilian Central Bank ("Managed Prices and the Inflation in Brazil", done by Francisco Figueiredo and Thaís Ferreira) verified that 49.1% of the

inflation from 1995 until 2002 was occurred due to the prices managed by government, although these prices is responsible for less than 30% of the formation of the inflation rate in Brazil.

So, the interest rates can reduce only a small part of the prices in the country: those determined in competition conditions. Therefore, the interest rates must be kept in very high levels, to strongly reduce the prices formed in competition conditions, in the attempt to keep the general inflation average inside the established goals. Thus, this monetary and cambial politics - high interests rates to try to control the inflation and to attract external capital to accomplish the external commitments - had a cost: the most bigger increase of the Brazilian public debt in our history.

The Country-risk stimulates the debt growth

The country-risk isn't a mechanism to prevent debt crises. In the truth, the "risk" stimulates the indebtedness process. The politics imposed by investors, such as privatizatioes, denationalization of our companies, high interests rates – stimulating the recession - and the free remittances to another countries (like profits and external debt interests) make the country more hostage of its indebtedness and risk evaluations. In the graph below, we show that Brazil, submitted to the neo-liberal politics, increase its remittances of profits and interests to another countries, since 1995, when the neo-liberal model was deepened by Cardoso's government. To send this money to another countries, we had to attract foreing capital, through external debt. We also note, in the graph, the big amount of interests remittances during the debt crisis, in the beginnig of the 80's, when Brazil was already under IMF supervision.



Source: brazilian Central Bank

The imposition, by creditors, of the high internal interest rates caused the exponential increase of the internal debt, and the recession, contributing for the growth of the debt/PIB relation. The imposition of the country-risk in the external debt bonds also causes uncontrolled growth of the external indebtedness, making difficult the debt payment by the indebted countries.

Conclusion

We verify, therefore, that the country-risk is a mechanism of spoiling the wealth of the Third World countries. We understand that, if the risk attributed by international agencies was not accomplished, and if we have been the best and more generous debt payers of the planet, what we pay due to the risk, in all these years, was IMPROPER and these payments must be considered as prepayment of the debt, reducing the value of the debt or being returned to the Third World countries.

On the other hand, we have to question the power of these international agencies of risk classifying, as well as the rules for its accounts. The biggest economic power of the world – US - is also the most indebted country and its risk is considered ZERO. Exactly after suffering violent terrorist attack and after several countable frauds in the biggest North American corporations, that are ECONOMIC AND FINANCIAL SCANDALS, and had caused enormous damages, the risk-USA continues ZERO! There`s much inconsistency in this parameter of the country-risk, that has damaging us seriously. The position where they classify Brazil is ridiculous, if compared with our condition of excellent payer.