

# WHEN THE MUSIC STOPPED:

Reagan Administration's Response to Brazil's Debt Crisis (1982-1983)

## QUANDO A MÚSICA PAROU:

*A resposta da administração Reagan à Crise da Dívida brasileira (1982-1983)*

Bruno Biasetto<sup>a, @</sup>

<sup>a</sup>Pesquisador do Centro de Estudos da América Latina e Caribe na New York University (Canadá). Doutor em História Econômica da América Latina pela Georgetown University (Estados Unidos).

@Contato principal: [bhb27@georgetown.edu](mailto:bhb27@georgetown.edu)

### Resumo

Este artigo acadêmico adentra a intrincada teia de manobras diplomáticas e legislativas orquestradas pela administração Reagan durante a crise da dívida do Brasil de 1982 e 1983. Focado na análise sobre como Reagan tentou evitar o calote brasileiro, o estudo analisa a formulação e execução de políticas, lançando luz sobre as delicadas negociações com o Congresso para a aprovação de um abrangente pacote de resgate em 1983. Em meio aos desafios apresentados pela interseção dos poderes executivo e legislativo na política americana, o artigo examina as complexidades de conduzir essas negociações. Além disso, analisa o papel desempenhado por instituições financeiras internacionais, como o FMI e o Federal Reserve, ao lidar com a crise da dívida da América Latina na década de 1980. Essa análise histórica ilumina as dinâmicas multifacetadas que moldaram a resposta dos Estados Unidos em um momento crítico na história econômica da América Latina.

### Palavras-chave

Crise da Dívida | Brasil | Reagan | América Latina | FMI

### Códigos JEL

F13 | F33 | F52 | H63 | N26

### Abstract

This academic paper delves into the intricate web of diplomatic and legislative maneuvers orchestrated by the Reagan administration during Brazil's debt crisis of 1982 and 1983. Focused on averting a Brazilian default, the study scrutinizes the formulation and execution of policies, shedding light on the delicate negotiations with Congress for the approval of a comprehensive rescue package in 1983. Amidst the challenges posed by the intersection of executive and legislative branches in American politics, the paper examines the complexities of navigating these negotiations. Additionally, it dissects the pivotal roles played by international financial institutions, such as the IMF and the Federal Reserve, in addressing the broader Latin American debt crisis of the 1980s. This historical analysis illuminates the multifaceted dynamics that shaped the United States' response to a critical juncture in Latin American economic history.

### Keywords

Debt Crisis | Brazil | Reagan | Latin America | IMF

### JEL Codes

F13 | F33 | F52 | H63 | N26

### Introduction

When the Mexican government sought assistance to address its external debt in 1982, few analysts could anticipate the unfolding events. Commencing in Mexico, the crisis soon permeated throughout Latin America, presenting one of the most formidable challenges to the Reagan administration in terms of American foreign relations. The IMF adjustment package, endorsed by the US government, emerged as a pivotal initiative in 20th-century American foreign policy toward Latin America. The measures implemented in 1983 by analysts from the Treasury and IMF would later influence the conceptual framework underpinning the Baker Plan (1985) and the Brady Plan (1989), ultimately inspiring what became known as the Washington Consensus.

This paper aims to dissect an issue that had a profound impact on Latin America, leaving an enduring mark on Brazilian society. In the early 1980s, Brazil found itself in need of credit from the IMF to service

its foreign debt. With the substantial contribution of the United States, the Fund's primary stakeholder, credit for servicing the debt in an orderly manner became available. The focus here is to scrutinize how the Reagan administration, Congress, and the IMF collaborated to avert a Brazilian default, which could have had severe consequences for American business interests in the region.

Given Brazil's status as both the largest debtor globally and the largest economy in Latin America, and considering the crisis occurred amid a complex political transition, it is logical to concentrate on Brazil. The paper initiates by recounting the acknowledgment of the crisis by the Brazilian military junta and delves into the origins of Brazil's debt during the 1970s. The subsequent section examines the political struggle within the Reagan Administration to secure congressional approval for a crucial rescue package to be administered by the IMF. Finally, the last section explores the approval of the package, the apprehension surrounding potential Brazilian rejection, and the significance of the 1983 adjustment package in addressing the debt crisis.

## 1. The Onset of the Crisis

December 20th, 1982 remains a significant date, albeit forgotten in the memory of most Brazilian historians. On this cold, cloudy day in New York, 1100 bankers from around the world, representing major creditors holding Brazil's external debt, convened at the Baroque Room of the Plaza Hotel. Their purpose: to hear from the Brazilian government about the repayment of their massive loans to the South American country. Brazilian authorities, alongside officials from the Federal Reserve (FED), International Monetary Fund (IMF), and Treasury, were hopeful that the bankers would accept the plan devised in October. Conversely, the bankers, discontented with the situation, believed the plan merely postponed an inevitable default.

At that juncture, Brazil's external debt was claimed by its government to be US\$ 72 billion, while creditors estimated it to be closer to US\$ 85 billion. With a current account deficit of US\$ 17 billion in 1982, Brazil was importing more than it could afford. Following extensive meetings in Rio de Janeiro and New York over two months, Brazilian and American authorities, aided by IMF experts, formulated a plan to avoid a collapse in 1983. The premise was simple: G-7 countries would extend additional credit to the IMF, enabling Brazil to service its debt. Simultaneously, banks would provide additional credit and reschedule payments due that same year. The package aimed to buy time for the Brazilian government to implement an extensive reform plan endorsed by the IMF and the American government (Veja, 1982).

The plan seemed theoretically sound, awaiting convincing all involved parties that it was the best and only solution for Brazil, Mexico, and other Latin American countries facing a similar dilemma. However, dissatisfaction among the bankers surfaced after the announcement at the Plaza Hotel. They found it incredulous that an extra US\$ 10.6 billion was sought from them merely to keep afloat the Brazilian government in the coming year. Moreover, there was skepticism about Brazil's ability to adhere to the austerity measures outlined by the IMF.

The international press echoed these concerns. The Economist, in its first edition of 1983, predicted that Brazil would need to implement economic measures so stringent that it risked pushing the country to the brink of social disorder. Referring to the story "Brazil Invents Sambatorium," the British publication outlined the necessity for severe deflationary policies, aiming to control government spending, reduce imports, and create a favorable environment for non-inflationary growth within two years (Economist, 1983). Numerically, this translated to cutting the current-account deficit from US\$ 17 billion to US\$ 7 billion in one year, reducing inflation from 100% in 1982 to a maximum rate of 57%, and growing exports more than fourfold to service the debt in 1983. This monumental task was even more challenging considering Brazil had officially been in recession since 1980, with unemployment exceeding 10% and negative GDP growth in 1981 and 1982 (Idem).

The exact magnitude of the financial hole remained uncertain. After allowing the IMF's analysts access to all ministry reports and statistics, a grim reality emerged. For over seven years, the government, despite high taxes and imprudent currency emission, had exceeded its means, unable to curb the spending spree of the 1970s (Veja, 1982). IMF findings at the Plaza Hotel revealed flawed public finance management, prioritizing the political objectives of the military rulers and their civilian supporters over maintaining a balanced budget (Economist, 1983).

In this tumultuous context, the United States government played a crucial role as a leader and mediator. The Reagan administration caught off guard by the magnitude of the crisis in Latin America since June 1982, when the Mexican government sought IMF assistance, coordinated its efforts through the Secretary of Treasury and the Chairman of the Federal Reserve. Secretary of the Treasury Donald Regan, inexperienced in international banking crises, faced challenges, compounded by the Reagan administration's initial "hands-off" approach (Carothers, 1991). Faced with the urgency of the moment, the United States government decided to mobilize its economic and political might to address the crisis from the outset.

By early 1983, the US government designated the IMF to manage the debt crisis in Latin America, mediating between the G-10<sup>1</sup>, bankers, and debtors. However, a significant obstacle loomed: the IMF's enhanced role required congressional approval, and the US government had decreased resources to multilateral banks since the Johnson Administration (Babb, 2009). Congress, having been told for over a decade that contributing to these institutions was a waste of taxpayer money, now needed to quickly approve funds during a colossal crisis.

Additionally, according to the IMF, Brazil alone required around US\$ 8.6 billion to avoid default in 1983 (Boughton, 2001). To allocate the necessary resources to the Fund, Congress had to give its approval. Simultaneously, the Reagan Administration needed to ensure Brazil's cooperation, realizing that the junta had to make substantial concessions to secure additional credit from the IMF (Ibid., p.278). Although Brazil had initiated a mild adjustment program to counter the effects of the Second Oil Shock, it proved inadequate, resulting in a severe recession in 1981 and 1982. President João Figueiredo (1979-1985), more concerned with the transition to democratic rule (*Abertura*), held onto developmentalist policies, making only minor corrections to address what appeared to be a temporary crisis. The Reagan Administration, however, favored radical market-oriented economic policies as the solution to Brazil's challenges.

## 2. Uphill: the battle for the IMF package approval

After his inauguration, President Reagan enjoyed a short honeymoon with the Congress. Reagan could pass one of his most significant accomplishments as President during this honeymoon period, the Economic Recovery Tax Act (ERTA).<sup>2</sup> The Republicans had the majority in the Senate, and the Democrats of the House of Representatives were not in a condition to challenge the popular President after the electoral debacle of 1980. By late 1982, the reality was different. A nation still mired in economic stagnation, a Democratic party emboldened by its victory at the 1982 mid-term elections and a weakened president transformed the Congress from a placid lake into a Roman arena.

One of the favorite areas where the Democrats were willing to challenge the President was foreign affairs. Democrats believed Reagan was a reckless cowboy who was willing to risk the world's existence in a final nuclear showdown with the Soviet Union. In this scenario, it was necessary for the party in opposition to challenge the President in every aspect of his foreign policy. Reagan's strategy to Central America became the favorite spot where the Democrats could make life difficult for the President (Arneson, 1989). The Boland Amendment, which tried to tie the Administration's hands in Nicaragua and culminated with the Iran-Contras scandal, is the clearest example of the troubled relationship between the two branches of

<sup>1</sup>The group of IMF's largest shareholders in 1983. They were composed by the G-7 countries, plus Switzerland, Sweden and Belgium.

<sup>2</sup>Economic recovery tax act. It was largest tax cut in United States history. It planned a 30 % across the board tax cut for all brackets. The cuts were given in three installments of 10 % a year.

power in foreign affairs.

Thus, when the Administration knew it would have to seek congressional authority to provide adequate resources to the IMF, it soon became clear that the task ahead would not be easy. The amendment to supply the IMF in the next fiscal changed the voting pattern of the House and Senate. During the nine-month debate about the issue, Congress did not split along the traditional lines of Republicans and Democrats. Three groups represented the opposition to the IMF funding bill. The first was the ultra-conservative Republicans from the Southwest, who were against the multilateral institutions perceived as a waste of critical national resources. Another opposition group was the supply-side zealots, led by Congressman Jack Kemp (R-NY), who believed market forces alone could address the crisis in Latin America. Kemp himself, one of the most reliable allies of the Administration, had already expressed his opposition to the IMF in an editorial for the *Wall Street Journal*. According to Kemp, any attempt to mediate the issue would only cost more money to American taxpayers and ultimately would not solve the crisis (Kemp, 1983). Finally, there were many Democrats who thought that an administration that was restricting credit at home to fight inflation should not provide cheap credit to indebted countries. On the other hand, a bipartisan legislative coalition of internationalists and friends of Latin America tried to secure the bill's approval.

For the initial hearing audiences at the Committee on Banking, Finance, and Housing Affairs that started on February 2nd, the Reagan administration decided to send two heavyweight officers: Paul Volcker (FED chairman) and Donald Regan (Secretary of Treasury) (U.S. Senate, 1983). They had a core message: the money was not for the IMF but ultimately aimed to promote American economic interests abroad. In a time when recovery at home was still feeble, exports to Brazil and Mexico alone supported approximately 225.000 American jobs. Therefore, keeping Latin America's most important economies afloat was essential, which was a sound economic policy that Congress could rally behind (Idem).

The Reagan administration also relied on a "shock and awe" element designed to scare Congress and secure funding at a faster pace. Both Volcker and Regan clarified that, given American banks' exposure to Latin American debt, these countries needed help. If the IMF did not have the extra funding to carry on with the task, default, and the American financial system's virtual implosion would soon follow. At the beginning of his statement, Paul Volcker said this was an "unseen situation in the postwar world." He also argued that the social tension in Brazil and Mexico was becoming unbearable, with people "eating out of cans." (Idem)

The scenario presented by Volcker was close to the Brazilian reality at that point. After getting US\$ 4 billion from the IMF as the first tranche of the help package, Brazil needed help to apply for the adjustment program. The deflationary policies to curb imports and restrain domestic consumption were taking a heavy toll on the Brazilian population. In 1982 alone, 700.000 workers lost their jobs and very soon started rioting and looting banks and supermarkets (Economist, 1983). Those still working had to live on a low wage, and inflation was severely eroding their purchase power. In cities like Rio de Janeiro and São Paulo, people were eating out of cans, as Volcker said. Brazilians were barely eating in the country's poorer areas, like the north and the northeast.

The FED chairman argued that only the plan designed by the IMF could take Brazil and Mexico out of that desperate situation (U.S. Senate, 1983). Moreover, it would not burden the 1983 budget since the resources to the IMF would come from government securities already in the FED's portfolio. That means the FED already had the funding available, and the operation would not increase the budget deficit. In addition, this credit to IMF was a loan to the Fund, argued Volcker. Ultimately, the IMF would send the money back to the US government, plus interest (Idem).

Despite the didactical tone of Volcker's statement, the representatives on the Committee were far from convinced of the importance of extending the IMF credit. What followed was a severe bombardment of the FED chairman and some heated exchange between him and the Representatives. Representative Henry Gonzalez (D-TX) feared the economic slump in Mexico could result in a communist revolution. Furthermore, such an event would oblige the United States to reshape its strategy, given the danger of having a communist regime next door. Other representatives like Stewart McKinney (R-CT) and Barney

Frank (D-MA) strongly criticized the Administration's rescue package by arguing that while there was no money available to implement recovery at home, there was ample federal credit for bankrupt Latin American nations (Idem). Congressman William Patman (D-TX) went even further, saying he preferred to see Volcker with the same level of concern about the ripping effects of high-interest rates at home. The vigorous attack on Volcker reflected the mood of the opposition towards Reaganomics at that point (Domitrovic, 2009). The Democrats were able to attach Volcker to Reagan, making them the symbol of everything that was wrong with the American economy at that point.

Having survived fierce attacks from members of Congress, Volcker might have thought that the calm inquiry conducted by Charles Schumer (D-NY) would be a respite from that ordeal. Schumer, in a cold, analytical way, got to the crux of the whole issue. Representative Schumer asked the FED chairman his thoughts on the evident contradiction behind the rescue plan rationale. Essentially, how the IMF and the FED expected to make Brazil repay its loans through export growth as both institutions advised deflationary policies (U.S Senate, 1983). Suddenly, Volcker was caught off guard and avoided a straight answer. He tried to dodge the question by saying that Schumer was wrong, and that the plan's success would prove that a balanced trade balance would, in the end, improve Brazilian exports, without going into specific detail on how that would happen. However, the problem was still there, and a small group of politicians and pundits started to ask themselves the same question.

One of the reasons Brazil had an enormous deficit in its current account was the need to import machinery from developed countries (mainly the USA) to improve its industrial plant and increase its exports. The orthodox plan designed by the Treasury and the IMF took much work to succeed in only one year. The main reason to insist on this unfeasible timetable was that the banks would never accept a "haircut" from the Brazilian government (Carothers, 1991). Hence, the country had to keep exporting at its maximum capacity to service the debt, at the expense of lower inflation rates. Furthermore, was the notion of a Brazilian moral hazard. The unofficial narrative in the US government and the IMF was that Brazil brought its problems on itself, and the banks were victims of reckless borrowing by underdeveloped countries. Therefore, Brazil deserved to be "punished" with adjustment while the banks deserved to be protected (Idem).

Donald Regan's statement, which followed Volcker's, emphasized the moral hazard argument. Before his testimony to the Committee, Regan defended his plan in an editorial for *The Wall Street Journal* (Regan, 1983), where he followed the same argument presented before the Committee:

- It was essential to ensure that it would be a long-term adjustment and not something only to address more immediate troubles.
- The IMF was the institution that would coordinate all the efforts to bring the crisis to an end and would enforce the adjustment programs.
- The creditors had to certify that these countries would adopt an economic model that could bring sustainable growth and free trade.

After that, Regan complained about the critiques against the bankers that were taking place on Capitol Hill. He said the banks could not have predicted that a prosperous country like Brazil would be in such a terrible situation. After all, the commodities market was booming during the 1970s, and Brazilian industrial exports were doing well; there were no indications that things would turn sour (U.S. Senate, 1983).

Regan preferred instead to blame the state expenditures and subsidies adopted by countries like Brazil to develop its infant industry. The Secretary of the Treasury was a banker with a solid devotion to the free market. Latin America's economic models based on Keynesianism were anathema to him. In Regan's view, protecting a weak industrial park did not make sense when Brazil's most vital asset was raw materials. In that sense, the crisis presented itself as an opportunity for the Reagan administration to push its economic model beyond American borders, and Brazil had everything to be the perfect showcase of the success of that formula.

By Arguing more on moral grounds than technical issues, Regan drew some support from the Senators in the Committee who agreed with him that Brazil had to give up on subsidies immediately. Industrial subsidies created problems for the Brazilian economy since they gave its industries a false sense of security and represented a colossal financial burden for the government. At the end of his statement, Regan reaffirmed that the commercial banks would provide the bulk of the rescue package, not the government. According to him, the banks offered a credit line of US\$ 13 Billion to Brazil (U.S. Senate, 1983). As a banker and member of a banker-friendly administration, Regan truly believed that his friends would not let him down and would stand by the Plaza Hotel agreement.

As the first quarter of 1983 ended, the situation was becoming increasingly desperate for Brazil. Congressional hearings on the extra funding for the IMF were still moving on in Washington without a definite date for a vote on the matter. Despite the plethora of panelists in four committees in the House and Senate arguing for the rescue package, the Republican leadership did not have enough support even in their party. Meanwhile, Brazil was trying to reach the goals set by the IMF. Despite its focus on boosting exports, Brazil mustered to export only US\$ 850 million in the first quarter of 1983, far behind the US\$ 1.5 billion it was needed (Economist, Apr.1983). Even worse was that even if Brazil could reach its goals, the IMF lacked the funds for the upcoming tranches of the emergency loan.

Opposition gained momentum as the Joint Banking and Finance Committee moved closer to a vote. Two of the bill's fiercest opponents, Congressman Ron Paul (R-TX) and Senator Jesse Helms (R-NC), strongly voiced their dissent. Ron Paul's main argument was that there was no crisis at all; this was an invention by the American bankers who only wanted to get a bailout from the American taxpayer (Joint Committee, 1983). Paul also believed that the IMF should disappear because it was an institution without any clear function after the end of the Bretton Woods system in 1971. Paul claimed his research proved that the debt of the Latin American nations was manageable, therefore banks and the indebted countries should solve that by themselves. Congressman Paul also believed the government's plan would only reward reckless behavior from a financial cabal. Finally, Paul argued that no matter what the FED or the Administration said, the bottom line was that the package would cost US\$ 8.4 billion to American citizens in a time of recession (Idem).

Three weeks after Ron Paul's statement, it was Jesse Helms' turn. The Senator was less vitriolic than Paul, but his criticism was equally harsh. Helms used a comprehensive compilation of data to prove his point. Senator Helms also affirmed that bankers were to blame for reckless lending in the Eurodollar market during the 1970s (Joint Committee, 1983). Helms also believed the package needed a thorough revision because of the conditionality principle attached to any IMF adjustment program. In that sense, the Senator argued that countries preferred to "give up the right to wage war than the right to inflate"; therefore, these countries would not follow the painful adjustment demanded by the Fund. In the end, Helms lost the composure he showed throughout his statement by ranting against the late John Maynard Keynes. Helms urged the Committee to seize the "opportunity" brought by the crisis to "get away from the Bretton Woods haunted house and from Lord Keynes ghost" (Idem). According to the Senator, the government had to emphasize privatization, free market, and deregulation as a precondition to approve the rescue package. Coincidentally or not, these words became the IMF's mantra for adjustment plans in Latin America since then. Regarding the debt crisis, Senator Helms argued that the IMF should sell its gold reserve to finance the rescue operation, not burden the American taxpayer (Idem).

From June 15th to July 21st, the Joint Committee for Banking, Finance, and Housing set up a panel about the situation of the Latin American economy. The Congress wanted to hear more from experts and panelists before casting a final vote in August. Raul Prebisch, the renowned Argentinian Economist of ECLAC (Joint Committee, 1983), gave one of the most revealing statements of that session. The ECLAC economist questioned the whole rationale behind the rescue package to Brazil and Mexico. Prebisch believed the economic imbalance would persist as long as the products from the developing countries did not have more access to the developed markets. Prebisch gave voice to a long-standing demand from developing countries that wanted new negotiations on the GATT agreement to ease market restrictions on their

products. Finally, Prebish also argued against the deflationary policies implemented by the IMF in Latin America and warned that people experiencing poverty could not stand such a burden anymore.

Prebish dismissed inflation as a serious problem and asked the US government to foster policies to bring growth to Brazil and Mexico. For him, the most important thing was not to fight inflation but to fight what he called "social inflation," which was the social inequality that existed in the region (Joint Committee, 1983). What Prebish said about the essence of the crisis would come to haunt the US government later, since the problem of inequality and the lack of growth hindered the effectiveness of the schemes designed by the IMF and the Reagan administration. On the other hand, his ideas greatly inspired Brazil's economic policies in the 1980s, with unfortunate results.

The Assistant Secretary of Commerce for International Economic Policy, Alfred H. Kingon, and Marc E. Leland (Assistant Secretary of the Treasury for International Affairs) gave their statements. Secretary Kingon explained that due to the economic downturn in Brazil and Mexico, American exporters had lost 335.000 jobs since the beginning of the crisis in 1982 (Joint Committee, 1983). This scenario hindered America's recovery from the recession. Kingon also stated that the crisis was an opportunity to foster foreign investment in Latin America because only private investment and market-friendly economic policies could solve their problems in the long run.

Marc E. Leland followed produced one of the most consequential statements of the hearings. Leland reaffirmed that the Reagan administration believed that the IMF was the centerpiece of the whole strategy to deal with the crisis. It was the only institution with the clout to solve the liquidity problem and implement long-term reforms simultaneously. Leland also assured that the steps to solve the crisis suggested by Secretary Regan would resolve the matter in a few months (Joint Committee, 1983). The US government wanted to promote a worldwide movement towards a healthier economic environment. This movement emphasized the primacy of market forces and free trade. In that sense, Leland rebutted Prebish by saying the IMF did not impose anything on anyone. In Leland's view, it was an institution that helped to identify and cure a country's economic ills. Finally, Leland also believed that Brazil would be back on its feet after five years of non-inflationary growth, which was the Administration's primary goal (Idem).

Both statements showed the Reagan administration's strategy to address the Latin American Debt Crisis. For these advocates of neoliberal economic policies, reshaping the American economy was only the beginning. For the Reagan Administration's economic advisors, the so-called "Reagan Revolution" had to be global (Harvey, 2005). Since its origins, the Neoliberal movement in economics grew from disgust of Keynesianism and its belief in the government as an economic agent. For the most fervent adherents, like Donald Regan and David Stockman, the 1980s was a turn point in the wipeout of Keynesian influence in developing countries (Frieden, 1987).

Therefore, the crisis in Brazil presented itself as an opportunity to implement a modernization program of such scale, one that would become the model for the entire continent. If a country like Brazil could succeed after adopting a market-friendly economic model, it would mean a considerable victory for the Reagan administration in its strategy for the Cold War. In contrast, Raul Prebish's thoughts represented mainstream economic ideas in Latin America. The Brazilian military junta liked those ideas because creating a national industrial sector and a solid and active State served well their nationalistic aspirations.

### **3. The end of the beginning**

By late June, despite the colossal efforts made by the Chairman of the House Banking, Finance, and Housing Committee, Fernand St. Germain (D-RI), and the White House, both sides of the aisle struggled to reach a consensus. Some Democrats did not see any sense in helping countries abroad while welfare was under attack at home. For most Republicans, giving money to "irresponsible" multilateral banks at a time

when the country was trying to keep its public spending under control was something close to lunacy.

Meanwhile, Brazil received the second tranche of the IMF's aid package following tense negotiations with the IMF, where Brazil threatened to default if the Fund did not soften its demands. Another US\$4 billion was supposed to keep the country in conditions to service its debt interest over the rest of 1983 (Boughton, 2001). However, the problem was that the Fund needed further funding to help Brazil in 1984 unless the US Congress approved the IMF quota increase.

In July, the Reagan Administration and the Republican leadership at Capitol Hill started to exert pressure on both Republican and Democrat members of Congress alike to approve the rescue package. Nevertheless, before the final vote, more panelists from the executive branch were summoned to testify to persuade Congress that the US\$8.4 billion package to the IMF should be approved. After numerous hearings, statements, and four amendments intended to kill the bill or expel the communist countries from the IMF, the bill was approved in the House in a very close vote, 221-217 (New York Times, 1983). The greatest disappointment for the White House was that the Republicans were the main hurdle to the approval, and nothing President Reagan had said seemed capable of changing their minds.

The close vote reflected the fact that several Congress members from both sides of the aisle were determined to avoid extending the IMF quota. Therefore, Reagan had to trust a few moderate Republicans and flirt with the Democrats. The Democrats wanted to approve a new housing bill worth US\$13 billion to guarantee their support for the IMF bill (New York Times, 1983). Budget director David Stockman hated the housing bill because he believed it would be a severe setback for a balanced budget in 1984. However, after much dithering, Stockman was overruled for political reasons, and the Housing Bill gained executive support—President Reagan signed the Germain Depository Institutions Act into law on November 30th, 1983. On the same day, Reagan also signed into law the new fund appropriation for the IMF. The Democratic vote guaranteed the bill's approval. Because of that, Reagan wrote a rare letter of appreciation to the Democrats on the Hill. Speaker O'Neill (D-MA) found the letter an "insufficient demonstration" of gratitude from the President (Idem). In summary, the opposition saved one of Reagan's most important foreign policy initiatives. There was a huge sense of relief at the White House, Wall Street, and Brasília. The Brazilian government had guaranteed credit to service its foreign debt in 1984, the American banking system would not collapse, and the IMF could push forward its reform initiatives in Latin America.

On September 13th, the House of Representatives debated an extra credit of US\$1.8 billion to Brazil through the Eximbank to boost American exports (U.S. House, 1983). Under the terms of this agreement, Brazilians could only use Eximbank's credit to buy manufactured products in the United States. This new proposal from the US government was supposed to have an easy time in that session because it helped American export industries struggling with the sudden loss of Brazilian demand. However, what happened was quite the opposite.

Alfred H. Kingon and William Draper III gave statements representing the Eximbank. Kingon affirmed that this credit line was necessary due to a 50% loss in American exports to Brazil in 1982 (U.S. House, 1983). According to him, this was a good policy that would not cost a lot and would positively affect many sectors of the American economy. William Draper affirmed that this was a "wise policy for the future", securing American interests in the region and boosting the economy out of recession. However, Draper admitted this was an Eximbank pet project without coordination with the IMF or the Secretary of the Treasury (Idem).

What followed was a fierce rebuttal from Congressmen Patman (D-TX) and Schumer (D-NY) against the Eximbank's project. Charles Schumer put the government officials in a difficult position by asking why the Eximbank was extending Brazil's credit line if the country was on the verge of a default (U.S. house, 1983). Moreover, if the IMF's whole adjustment program compelled Brazil to import less, why were they giving them credit to import more? Congressman Patman further affirmed that the Eximbank had to be extinguished for moving forward with "reckless practices." Draper and Kingon were in a difficult position to explain what seemed to be a dysfunctional policy by the US government. Both Draper and Kingon reaffirmed a core argument of the Reagan Administration: Brazil's economic destiny lay with the



United States (Idem). Theoretically, the Eximbank plan could work, but it could boost inflation and make Brazil's external debt even higher levels. In 1984 and 1985, Brazilian industries imported more from the United States, and while the economy showed a higher activity level, the predictions about inflation and the external debt unfortunately proved to be right.<sup>3</sup>

The confusion around the Eximbank loan demonstrated that the White House was at loggerheads during the planning stages of the rescue package. As pointed out by Carothers (1991), the US government struggled to put place a coherent strategy for the economic crisis in Latin America. Overall, there was an appearance of coordination that masked the fact that the Administration was pursuing economic policies that ultimately contradicted the goals they wanted to achieve. All the parties involved agreed that Brazil needed to have a lower inflation rate and avoid a default. Moreover, all the parties involved also knew that Brazil had to implement deflationary policies to have lower inflation rates and, therefore, had to import less. In that sense, the Eximbank loan ran against the main goals set by the Administration.

Meanwhile, the United States was trying to boost its exports to Brazil in the hope that with this loan from the Eximbank, the Brazilians would achieve their importation quotas by buying less from other nations. Another issue was the belief that the crisis was only a liquidity problem, not an insolvency one. This mistake by the White House made the first help package to Brazil something of an inefficient tool to deal with a crisis of this magnitude. Countries like Brazil and Mexico were able to service their debts efficiently if offer the right conditions to do so. However, they were instead facing challenging structural issues beyond the prophylactic measures proposed by the US government at that moment.

September 28th marked the Reagan Administration's last stand to persuade Congress that Brazil was coming out of the crisis. In a special panel about the Brazilian crisis, some administration officials tried to make the case for the help package to Brazil and why it was essential to keep funding the IMF. Fred Bergsten, a former Carter administration official, stated that "Brazil had everything to thrive" and was very optimistic about the country's future (Joint Committee, 1983). Bergsten also argued that the IMF's reforms aimed to fix the main issues that had led Brazil to this dismal situation. In his view, the Brazilian government had to be supported by the IMF to fight excessive public spending and wage indexation, both seen as the leading causes behind hyperinflation and high debt levels (Idem).

By the end of his statement, Fred Bergsten warned that Congress was risking repeating the tragic consequences of the Smoot-Hawley Act<sup>4</sup> if it opted not to help the developing countries engulfed by the Debt Crisis. Without the approved bill supporting the IMF, there was a high risk that a systemic default would have followed. Furthermore, given the level of exposure of the leading American banks to the Latin American debt (50-75 % of their capitalization), a local crisis could soon become a global crisis of immense proportions.

The tone set by Fred Bergsten prevailed on that day. It was an interesting mixture of scare tactics with effusive optimism. Jack Guenther, vice president of Citibank, followed the same argument. Guenther argued that Brazil had faced a similar situation before when the country faced the threat of an economic meltdown during the early 1960s. After the military junta seized power in 1964, the United States and Brazilian technocrats put an adjustment plan in place. The Campos-Bulhões plan was able to restructure Brazil's economy and set the stage for the "miracle" of the 1970s. In supporting the IMF, the United States believed it would give the Fund the tools to reenact this successful initiative.

Anthony Motley's statement was the high point of the hearing session that day. Motley was the Ambassador to Brazil until late 1982 when he returned to Washington to serve as Assistant Secretary of State for Inter-American Affairs. Moreover, Motley was born in Brazil, spoke Portuguese fluently, and was a very close friend of President Figueiredo (1979-1985). First, Motley exalted the Brazilian military junta's ability

<sup>3</sup> By 1984 and 1985 with the beginning of the Reaganomics boom, American demand for Brazilian products increased sharply. This trend made the Brazilian government more optimistic about its economic outlook and less willing to implement the fiscal adjustment demanded by the IMF. While the influx of US Dollars improved in 1984, Brazil was also importing more to cope with foreign demand. Unfortunately, higher demand made inflation to soar from 115.1 % in 1983 to 141.2 % in 1985 (IMF,1988).

<sup>4</sup> The Smoot-Hawley Tariff Act of 1930 was a piece of U.S. legislation that significantly raised tariffs on a wide range of imported goods. The primary aim was to protect American industries by making foreign goods more expensive and thus encouraging domestic production. However, the Smoot-Hawley Act had unintended consequences and is widely regarded as exacerbating the Great Depression. In retaliation, many trading partners imposed their own tariffs on American exports, leading to a global trade war. The increase in protectionist measures contributed to a decline in international trade, deepening the economic downturn.

to keep order and promote economic development at the same time since 1964. His words emphasized the idea that the regime deserved a vote of confidence from the American government for being such a dedicated ally against communism in South America (Joint Committee, 1983). Motley also argued that Brazil's economic growth in the 1970s ceased after the Oil Shock of 1973. In his view, since Brazil had to import about 80% of the oil it used for domestic consumption, the country was heavily exposed to the sharp increase in oil prices. The former ambassador also believed that a series of unfortunate events like meteorological phenomena and political changes abroad put the country in its present situation.

During his statement, Motley was interrupted by Senator Charles Mathias (R-MD), who asked to comment. Mathias was with President Reagan when he visited Brazil in December 1982. Senator Mathias was fascinated by the country and, at the same time, puzzled by its desperate situation. Motley's rebuttal to the Senator's comment was that the "only flaw" of the Military junta was not to embrace market-friendly economic policies (Joint Committee, 1983). According to Motley, the country needed to get public spending under control, and the best way to do it was to privatize state companies. He regretted that the first round of privatizations had not attracted any buyers because the Brazilian government only offered less attractive companies. The big prizes, Petrobras (oil) and Vale (iron ore), were still under the strong arm of the State. Senator Mathias also expressed dissatisfaction with a country of continental dimension and rich in natural resources that refused to open itself to the "benefits of the free market." Both agreed that the solution to Brazil's ills was to adopt the neoliberal recipe the Reagan Administration proposed (Idem).

It is important to emphasize here how the literature on the topic usually affirms that privatization appeared in Brazil only after 1989, with the Washington Consensus (Mercadante, 1997). Based on the testimonies given to Congress, it is possible to infer that the US government and the IMF have been pushing for a comprehensive privatization program in Brazil, at least since 1981. However, in the junta, there was little support for privatization, mainly because it ran counter to its nationalistic politics. For most of the population and the influential civil servants' labor unions, privatization was anathema as well. The topic of privatization would be a considerable point of contention between the Brazilian government and the IMF during the 1980s. What is certain is that neither the Brazilian government nor its civil society was ready to accept such a drastic measure.

Finally, Motley told Senator Mathias he should not worry about social chaos. It would not happen in Brazil because, according to him, the "Portuguese stock was different from Spanish stock." Also, the Portuguese who colonized Brazil did not have the same "hot blood" as their South American neighbors whom Spain colonized (Joint Committee, 1983). In his view, this factor alone made Brazil less prone to revolutions than the other Latin American countries. Despite Motley's optimism, looting was happening in all major Brazilian cities at that point. Although 2/3 of the population was suffering from malnutrition and millions more were unemployed, a large-scale popular uprising was unlikely. As the return to democracy was moved forward, it was not in the opposition's interest to foment a revolution and risk a military backlash.

#### **4. Conclusion**

In December 1983, President Reagan wrote in his diary: Brazil accepted IMF terms—good news for the world financial markets (Reagan, 2007). The British magazine "The Economist" published a story about the first Christmas of the crisis in Brazil (Economist, Dez 1983). It summarized all the challenges faced by the country during a tough year. That included the complex negotiations in Washington, the IMF's threats to cut Brazil's emergency loan, and the urban riots. Finally, the magazine concluded that Brazil would have a difficult 1984, but it was unlikely to be worse than 1983. The optimism of Christmas soon faded away, and 1984 brought even higher inflation and several quarrels with the IMF due to unfulfilled reform promises on Brazil's part.

Despite the severity of the Debt Crisis, Brazil did not fall apart, and power returned to civilians in 1985. The merry-go-round surrounding the debt and the lackluster economy culminated in 1987 when President José Sarney (1985-1990) declared a unilateral moratorium on the country's external debt. Not even the most pessimistic analyst of the Brazilian crisis would have imagined it would take until 1994 for the country to get inflation under control. It is essential to point out that several plans approved by the IMF in the 1980s failed, and the plan that the IMF did not approve was the one that solved the problem. Paradoxically, many 1983 adjustment plan features were in the successful Real Plan (1994). Both plans shared important characteristics of privatization, combating inflation, and the insertion of the Brazilian economy into the global market. What went wrong in 1983 that worked in 1994? In a nutshell, by 1994, Brazil had a civil society ready to accept structural changes to put inflation under control.

As often happens in American politics, the troubled relations between the executive branch and Congress are crucial in shaping foreign policy. The struggle of the Reagan administration to put in place a coherent policy to deal with the Latin America's debt crisis was no different from the current conundrum surrounding financial support to Ukraine and Israel. Moreover, the brain thrust behind the American plan was flawed: this was not a liquidity crisis but an insolvency crisis, as it became evident as high inflation and debt remained strong throughout the 1980s. Another mistake was Reagan's supply-side zealots' belief that Brazil and other Latin American countries would accept sweeping economic changes immediately, disregarding the potential political repercussions of those changes. The Reagan administration also misread the banker's intentions when they thought American banks would help the IMF by extending credit lines and more generous debt rescheduling programs to Brazil. None of this happened, and the risk-averse banks made the US government and the IMF take the toll.

Moreover, the prospect of Wall Street bankers confronting substantial losses was abhorrent to the White House, rendering a more straightforward resolution improbable for the debtors. Additionally, the long-standing Congress aversion to multilateral institutions persisted. The notion of rescuing banks and foreign competitors while the United States grappled with recession appeared nonsensical to several members of Congress spanning the political spectrum. Despite skepticism from a segment of Congress, the genuine threat of a global depression stemming from the financial collapse of American banks exposed to Latin American debt loomed large. However, isolationists deemed the risk worth adhering to their principles. It required a significant effort from the executive branch and substantial concessions to Democrats to materialize the IMF bill. Unfortunately, within six months of its approval, it became evident that the bill had failed to properly address the Debt Crisis.

## 5. Bibliography

ARNSON, C. **Crossroads : Congress, the Reagan administration, and Central America**. New York: Pantheon Books, 1989.

BABB, S. L. **Behind the development banks : Washington politics, world poverty, and the wealth of nations**. Chicago: University of Chicago Press, 2009.

BOUGHTON, J. M. **Silent revolution : the International Monetary Fund, 1979-1989**. Washington, D.C.: International Monetary Fund, 2001.

Brazil invents the sambatorium. **The Economist**, p. 69, 8 jan. 1983.

Brazil's pulse is weak. **The Economist**, p. 72, 16 abr. 1983.

CAROTHERS, T. **IN THE NAME OF DEMOCRACY :u.s. policy toward latinamerica in the reagan years**. S.L.: Univ Of California Press, 1991.

Crise da dividachegaaBrasil. **Veja**, 22 dez. 1982.

DEVLIN, R. **Debt and Crisis in Latin America The Supply Side of the Story**. [s.l.] Princeton

University Press, 1993.

DOMITROVIC, B. **Econoclasts**. [s.l.] Simon and Schuster, 2023.

FRIEDEN, J. A. **Banking on the World**. [s.l.] Wiley-Blackwell, 1989.

GROSH, M. E. **Social Spending in Latin America**. [s.l.: s.n.].

HARVEY, D. **A Brief History of Neoliberalism**. Oxford: Oxford University Press, 2005.

IMF. Empirical Analysis of High-Inflation Episodes in Argentina, Brazil, and Israel. **IMF Working Papers**, v. 1988, n. 068, 1988. Disponível em: [www.elibrary.imf.org](http://www.elibrary.imf.org). Acesso em: 18 jan. 2024

JAMESON, K. P. **Latin America in the 1980s**. [s.l.: s.n.].

JOHNSON, H. **Sleepwalking through history : America in the Reagan years**. New York: W.W. Norton, 2003.

JOINT COMMITTEE on Banking, Finance and Urban Affairs. Session on Brazilian Foreign Debt, September 28 1983.(Accessed: March 24, 2023). Text in: ProQuest® *Congressional Hearings Digital Collection*. IMF quota increase, minority view, 03/05/1983, (Accessed: March 25, 2023). Text in: ProQuest® *Congressional Hearings Digital Collection*.

HELMS, J. In a pinch, the IMF could go for the gold. **Wall Street Journal** (New York), May 6, 1983, p. 28.

KEMP, J. The solution to the World debt. **Wall Street Journal** , 2 fev. 1983.

LANDY, T. M. **From Miracle to Crisis**. [s.l.: s.n.].

LEOGRANDE, W. From Reagan to Bush: the transition in US policy towards Latin America. **Journal of Latin American studies**, v. 22, out. 1990.

MERCADANTE, A.O. **O Brasilpós-real**. [s.l.] Universidade Estadual de Campinas Instituto de Economia, 1997.

MIDDLEBROOK, K. J.; RICO, C. **The United States and Latin America in the 1980s**. [s.l.] University of Pittsburgh Pre, 1986.

MORLEY, S. A. **Poverty and Inequality in Latin America**. [s.l.: s.n.].

BRESSER, C. **A Turning Point in the Brazilian Debt Crisis**. [s.l.: s.n.].

PSACHAROPOULOS, G. **Poverty and income distribution in Latin America : the story of the 1980s**. Washington, D.C.: World Bank, 1997.

REAGAN, R. **The Reagan Diaries**. [s.l.] Harper Collins, 2007.

REGAN, D. The United States and the world's debt problem. **Wall Street Journal**, 8 fev. 1983.

RHODES, W. **Banker to the World: Leadership Lessons From the Front Lines of Global Finance**. [s.l.] McGraw Hill Professional, 2011.

ROJAS-SUÁREZL.; STEVEN RIESS WEISBROD. **Financial fragilities in Latin America : the 1980s and 1990s**. Washington, Dc: International Monetary Fund, 1995.

SLOAN, J. W. **The Reagan Effect**. [s.l.: s.n.].

Turning wine into water. **The Economist**, p. 4, 12 mar. 1983.

Twelve months later, Brazil prepares for Christmas, 1982. **The Economist**, December 17, 1983. *The Economist Historical Archive* (accessed January 11, 2024), p.87-88. [link.gale.com](http://link.gale.com)

U.S. HOUSE. Committee on Banking, Finance and Urban Affairs. Eximbank. September 13-14 1983),(Accessed: March 23, 2023).Text in: ProQuest® *Congressional Hearings Digital Collection*.

U.S. SENATE. Committee on, Banking, Finance and Urban Affairs. Donald Regan Statement, February 2-91983, (Accessed: March 25, 2023). Text in: ProQuest® *Congressional Hearings Digital Collection*.

Paul Volcker Statement, February 2-9 1983. (Accessed: March 24, 2023).Text in: ProQuest® *Congressional Hearings Digital Collection*.

VOLCKER, P. A.; TOYOO GYOHTEN. **Changing Fortunes**. [s.l.] Crown, 1992.

WIARDA, H. J. **American Foreign Policy Toward Latin America in the 80s and 90s**. [s.l.] NYU Press, 1992.

WRISTON, W. B. **Risk & Other Four-letter Words.** [s.l: s.n.]