Folder for reading on Thursday
AT 14/9

2

PRIME MINISTER

INTERNATIONAL BANKING CRISIS

Sir Walter Salomon says that before you went on holiday he sent you a paper of his on how to solve the international banking crisis. I do not remember seeing this though you may have received a copy directly. If not I now attach a copy.

Sir Walter has asked whether you would like to

i) Comment on his paper?

ii) See him prior to the International Banking Conference starting at the end of next week?

Before you can comment or discuss this with him I think you need an analysis from the Treasury/Bank of England.

Agreed
MT

Briefly, the proposal seems to involve the establishment of an agency under the BIS which would take over non-performing debts from the banks. The agency would negotiate with the debtor countries a longer repayment schedule and a more favourable interest rate which would be made possible by financial assistance from the industrial country governments. The loans would be secured on assets in the debtor countries and when the loans had been put on a sound basis they would be sold by the agency to financial institutions and the proceeds realised would be returned to the lending bank. If this happened, the lending bank, if there was any shortfall, would have to write off the difference. Since governments would be making available finance to enable the debtors to service their debt through what Sir Walter calls tax credits (he does not explain what tax the credit is against) there is a possibility that the loans would be kept near their face value.

Subsidy

!

Sir Walter claims this is the first proposal from an experienced, practical banker though there is no substance whatsoever to this claim. The scheme incorporates many of the elements which appear in the other fifty or so schemes which have been identified. It is a comprehensive, rather than a case-by-case, solution which involves the creation of a new international agency. It requires financial support by governments, it involves the securing of loans on LDC assets and incorporates a market for debt.

In my view, it omits one important element in the debt problem. Most of the debt was attracted in dollars on variable rate interest terms. As a result of US fiscal policies, the debtor countries have suffered a double penalty. Not only are interest rates much higher than expected but the burden of the debts is much greater than expected. To repay a given quantity of dollars, the debtors have to export much greater quantities of goods. The beneficiaries of this are those who deposit dollars with the banks and have seen the value of their deposits rise dramatically in terms of other currencies. Following the rise in the oil price in 1973-74, the burden of debt of the oil importing countries was reduced by the weakness of the dollar and by world inflation; after 1979 the opposite has happened.

Agree we tell Sir Walter:

i) That you have asked for an analysis of the paper? Yes

ii) That you are not yet in a position to comment? I would rather wait for that before commenting. The analysis had not been done before as he had asked me to keep the previous paper strictly confidential not

~~iii) That you will not be able to discuss this with him, given your diary,~~ before his Conference at the end of next week?

I willing to see him

When we have comments we can decide whether you should see Sir Walter or write to him.

AT

13 September 1984

lile BM

10 DOWNING STREET

From the Private Secretary 13 September 1984

Dear David,

INTERNATIONAL DEBT

I wrote to you on 6 June about a proposal which Sir Walter Salomon had put to the Prime Minister for resolving the international banking crisis. He has now set out his proposals in more detail in the attached pamphlet. I would be grateful if you could commission an appraisal of this proposal. In particular I am puzzled by the proposal for special tax credits. It is not clear what tax these are credits against but the purpose seems to be for Western governments to provide some financial asssistance to the debtor countries to enable them to meet their debt service payments. Also I am unclear about the way a bank would account for a loan while it was temporarily with the Realisation Company being put onto a sound financial basis. Does the bank assume that the full value of the loan will be realised or does it assume that the whole loan should be written off, with anything that is realised being treated subsequently as a bonus?

BM As Sir Walter is pressing the Prime Minister for a reaction, I would be grateful if a note could reach me by Thursday of next week.

I am copying this letter to John Bartlett (Governor of the Bank of England's office).

Yours sincerely
Andrew

(Andrew Turnbull)

David Peretz, Esq.,
HM Treasury

EC

1. MR. TURNBULL

2. PRIME MINISTER

Before you went on holiday Walter Salomon sent you a paper on how to solve the International Banking Crisis. I attach a copy.

Sir Walter wonders whether you would like to:-

(i) comment on his paper.

(ii) see him prior to an International Banking Conference starting at the end of next week.

CR.

12 September, 1984

This paper is intended to provoke thought and discussion and suggest a constructive framework. It is not a blueprint and should not be regarded as such. However, if the basic ideas are accepted, the technical details can be worked out by a team of experts including, where necessary, international lawyers and accountants.

Sir Walter Salomon

The International Banking Crisis:

A new approach by Sir Walter Salomon

The Salomon Plan

THE AUTHOR

Sir Walter Salomon was for many years Chairman and is now President of Rea Brothers Plc, the private bankers. He comes from an old Hamburg banking family and having witnessed the havoc caused by the German inflation of 1923-24, escaped from Hitler to Britain in 1937.

He is life president of the Young Enterprise movement which he founded and a Freeman of the City of London. He was knighted in 1982 and has had conferred on him the Brazilian Order of the Cruzerio do Sul and the Officer's Cross of the Order of Merit: First Class (Federal German Republic). He has written on current affairs topics for many years and previous publications include 'One Man's View' (1973) and 'Fair Warning' (1983).

CONTENTS

SUMMARY

—Lenin predicted that capitalism 'would destroy itself through the disintegration of the monetary system'. We are now on the brink of such a collapse.

—It is said that 52 propositions have been put forward to solve the international banking crisis, but none by an experienced, practical banker.

—Papering over the cracks, as with the nationalisation of Continental Illinois Bank, is not the answer. This merely means that some banks are bailed out at the expense of others (some would say this amounts almost to a fraudulent preference) and that many of those responsible in the offices of the banking supervisory authorities keep their jobs. This is an example of the stupidity of tackling the effects of the crisis rather than the fundamental causes.

—The people who created the crisis cannot solve it—the blame lies with governments and politicians, central banks and commercial banks. The solution must be taken out of their hands.

—The problem cannot be dealt with nationally but must be handled on an *international* basis.

—Confidence can only be restored with a constructive approach—the proposals are not designed to undermine the present system but to save it, although in the process some well known banking names may disappear.

—Responsibility for the present crisis should not be taken by the less developed countries alone. In some instances loans were pressed on them for political reasons. In any case a number of these countries have already made Herculean efforts to avoid default.

—Whilst most less developed countries are insolvent in the sense that they run serious current account deficits, many of them are enormously rich in raw materials, mineral reserves, etc. These resources should be mobilised for the benefit of the countries concerned as proper risk collateral.

—A scheme in excess of the scale of the post-war Marshall Plan is required, although this time the benefits should not be squandered on social experiments but applied to regaining financial equilibrium.

—All non-performing loans should be transferred from the commercial banks into the temporary stewardship of an International Realisation Company. The trustee should be the Bank for International Settlements.

—There would be no advantage for any individual bank refusing to join the scheme, as the regulatory authorities would disregard any doubtful loans in calculations of capital ratios for solvency purposes.

—In order to relieve the desperate financial plight of the less developed countries, Western governments must enable interest rates on borrowing to be cut by abolishing tax on such receipts provided the entire benefit of the abatement is passed back to the borrowers. In these circumstances it may also be possible—and certainly desirable—to establish sinking funds.

—The Realisation Company would be empowered to reorganise and repackage non-performing loans with a view to realising them on behalf of the banks. This would be done either by selling them on an open market basis or by arranging for re-payment or re-scheduling according to strictly traditional banking criteria.

—The Realisation Company would need to be given absolute immunity from any kind of litigation by the banks, their shareholders or other third parties so that it could act independently. In effect it would act like a liquidator of a private business.

—All new loans to less developed countries would have to be arranged on normal commercial terms with adequate security. Sovereign guarantees would not normally be sufficient collateral. Restrictions on foreigners taking charges on assets situated within national boundaries should be lifted.

—Banking supervision shall be taken out of the hands of those national central banks which lack independence from political interference and are bureaucratic in approach.

—If governments want commercial banks to give credits for political reasons they shall provide guarantees so that if they are not repaid the government concerned would be liable.

INTRODUCTION AND BACKGROUND

In 1971 in a speech given to the Institute of Bankers in London I said there had been certain developments in the eurodollar market where 'some of the good old banking principles had been sadly neglected . . . there is also growing concern that perhaps the condition of the borrowers is not always examined as closely as might be desirable . . . if there should be a serious disturbance, it might lead to most undesirable consequences in the international money market'. Then in 1976 I wrote: 'I can foresee the day, if it is not already here, when many of these (developing) countries will not be able either to service the loans or make repayments on the due date'.

I would also draw your attention to Lenin's chilling prediction that capitalism 'would destroy itself through the disintegration of the monetary system.' In May the eighth largest bank in the United States, the Continental Illinois, collapsed because its depositors lost confidence in its soundness. Two months later the American government itself was forced to take over Continental Illinois's bad loans in the most expensive bank rescue in American history. At the same time the world's major debtor countries in Latin America have been indicating that high US interest rates are making it impossible for them to service more than a tiny proportion of their loans.

These countries owe more than $40 bn to the top nine American banks, whose capital and reserves total only $31·5 bn; likewise British high street banks are owed a sum by these same debtors that also exceeds their capital and reserves. To put the matter bluntly, many large international banks are insolvent because they have lent on a vast scale to countries in Latin America and elsewhere which cannot repay their debts in any conceivable circumstances.

There can be no justification for empty discussion that undermines confidence because a credible plan designed to restore equilibrium is lacking. Naturally governments and central banks have said as little as possible about the matter because they have been concerned to preserve faith in the existing system. But I am reminded of the atmosphere in 1938 and 1939 just before the last war. Everyone knew conflict was coming but somehow nobody seemed able to do anything to prevent it. I am informed that behind the scenes no less than fifty-two propositions have been put forward to solve the problem. However, to my knowledge not one of these fifty-two has been put forward by an experienced banker.

Meanwhile, Mexico, Brazil and some of the other countries involved have made heroic efforts to meet their obligations by blocking off all but the most essential imports, by forcing substantial cuts in real wages on their people and by acquiescing in increased unemployment although social security is rudimentary if it exists at all. But on the most optimistic forecasts these countries cannot expect to attain surpluses on their current accounts sufficient to meet their debt obligations even in their 'restructured' form. They have stated that high US interest rates are making it impossible for them to service more than a tiny proportion of their loans. Nor can political problems be ignored. Brazil and Argentina, for instance, are both attempting the tricky passage from military dictatorship to Western style democracy. They are thus simply incapable of imposing an IMF deflation on their people. Argentina has publicly discussed the advantages and disadvantages of default.

Many estimates have been made of the exposure of leading American and British banks to Latin American risks alone; the calculations have been based on the reasonably full information which the banks themselves disclose. The results invariably show that many banks have lent significantly more than an amount equivalent to their capital and reserves to Latin America. In May this year, for instance, the Federal Financial Institutions Examination Council in the United States showed that the nine largest American banks had loans totalling \$40·4 bn outstanding to Mexico, Brazil, Venezuela and Argentina compared with a combined capital of \$31·5 bn. In July, the London stockbroking firm of Panmure Gordon & Co. published tentative estimates for the British Big Four banks showing that as a group they had lent £12·8 bn to Latin America compared with total capital of £8·9 bn.

...n on favourable assumptions about the amounts of bad debt already 'written off' and the residual value of the great bulk that remains, nobody can doubt the conclusion that a number of important banks are effectively bust.

In 1975 I wrote an article which was published simultaneously in *The Times* in London and *Die Welt* in Germany called 'Bonds for the Arab Oil Funds' and in 1983 an article called 'Origin and Cure of the International Banking Crisis'. I have included both these articles as appendices to this discussion paper so that you can see that my proposals are not dependent upon *hindsight.*

Last year when I attended the Per Jacobsson Lecture at the IMF Meeting in Washington, there was a question and answer period at the end of the lecture. My question to the speaker, Mr H. Johannes Witteveen, was whether he agreed that some of the leading bankers had been acting irresponsibly, and furthermore, whether we had any guarantee that they would not do so in the future. After some thought, his reply was that this might be so with hindsight. I subsequently told him that in my opinion it showed a lack of foresight! Anyone in doubt about the views I have expressed in the past needs only to re-read my books 'One Man's View' and 'Fair Warning'.*

* 'One Man's View' and 'Fair Warning' are published by Churchill Press, 2 Lord North Street, London SW1, price £2·00 and £5·95 respectively.

THE EVENTS LEADING TO THE PRESENT CRISIS

I place the blame for what has gone wrong on governments, politicians, the central banks and the commercial banks. The politicians encouraged the notion from the time of the first oil shock onwards that commercial banks virtually had a duty to engage in what was known as 're-cycling'. In other words the unspendable surpluses of the oil exporting countries were to be taken in as deposits and on-lent to the countries that were most severely punished by the rise in oil prices, the rest of the third world. But in giving this encouragement politicians blithely ignored the risks to both sides of a bank's balance sheet. Put simply, the nature of the deposits was unsuitable for the type of borrowing facilities demanded by the third world countries. Finance ministers and officials of Western governments were often unduly influenced by the highly intelligent and persuasive ways in which representatives of developing countries always present their case. Aid was demanded by right and with no strings attached; requests for bank finance were couched in much the same terms. I dare say, too, that Western governments were tempted into promising developing countries extra loans at favourable terms in return for, say, votes at a forthcoming meeting of the United Nations.

I also blame the central banks for the present crisis. I have long regretted the nationalisation of the central banks of the Western world and their loss of independence. Central banks are one of the natural checks in the financial system; by weakening their authority we make it more difficult to prevent excesses developing. Where once they looked after the interest of the bankers, they have become subject to the whims of politicians. They can be forced to carry out a policy dictated to them by government with which they instinctively disagree. Central bankers no longer deserve the title; they have become government officials. Who can now doubt that Western central banks and other agencies charged with supervising commercial banks have failed to meet their responsibilities?

of progressive deterioration in bank balance sheets has taken place under their very eyes. The U.S. Comptroller of the Currency who first discerned weaknesses in Continental Illinois' position in 1981 is still at his post assisting with the biggest bail out in American banking history. While small banks often find central banks unduly obstructive, large banks have been allowed to carry on regardless.

It is instructive to look a little more deeply into the background of the nationalisation of Continental Illinois. This bank crashed primarily because it purchased a dud loan book from another bank, Penn Square Bank of Oklahoma. It is clear that normal banking criteria had not been applied and although the authorities were alerted to the problems of Penn Square in 1981 and its chief, energy lender was known to wear a Batman mask to the office and drink liquor out of his shoes, nothing was done until it was too late.

By 1982 Continental had plunged into substantial losses, despite which the Chairman maintained that he still believed his bank's lending techniques were 'basically correct' adding 'we have no intention of pulling in our horns.' The bank remained 'strong, financially sound and stable,' he claimed. Confidence, however, which is a bank's most precious possession, had been fatally damaged. Statements about pressing on regardless provided no reassurance.

Soon afterwards the bank sold its credit-card business to raise capital. Yet rumours that the bank was in severe difficulties began to circulate. Breaking with all precedent, the United States Comptroller of the Currency issued a statement.

It could hardly have been more definite, or reassuring. The Comptroller said that his agency was 'not aware of any significant change in the bank's operations as reflected in its published financial statement that would serve as a basis for these rumours.' And he added, for good measure, that the bank's financial ratios compared favourable with others. A few days later sixteen rival banks arranged a standby credit for Continental Illinois amounting to \$4·5 bn.

All to no avail. Once confidence in a banking institution is fractured, it cannot be restored by statements representing no more than wishful thinking, whoever might issue them. Exactly seven days after the Comptroller had said his piece, the American authorities had to give the bank a further $2bn infusion of emergency finance. The new Chairman said: 'This positive step . . . provides us with the resources needed to do business and once and for all should and must stop the rumours.' Moreover, the Chairman of the Federal Deposit Insurance Corporation promised domestic and foreign depositors that 'they will not suffer loss.'

It made no difference. The bank could not prevent deposits draining away. So, finally, it was announced that the Federal Deposit Insurance Corporation would take control of the bank, appointing as it did so another set of top executives. The conclusion is that as confidence could never be re-established and the bank is a large one, it eventually had to be nationalised—and by a government to which such a move is particularly abhorrent.

Rather than attending to fundamental weaknesses in bank balance sheets, central banks have taken the lead in positively encouraging banks to make available further sums to the debtor countries as part and parcel of re-scheduling agreements. The only logic in lending more money to borrowers who have admitted that they cannot pay what they already owe is that it allows banks to pretend that they are still receiving interest on their loans. This spurious fact in turn enables the banks to persuade their auditors that these loans can still be classified as sound in their balance sheets. That central banks can play a leading role in such a charade is one of the more regrettable aspects of the crisis.

Finally the leading international banks themselves must carry a large responsibility for what has gone wrong. Re-cycling literally billions of dollars fitted in with the league-table mentality of many of them. They became obsessed with growth and with overtaking their rivals. The extent of their balance sheet footings was more important to them than what is prudent and what is not.

More to the point, the managers of these burgeoning commercial banks seemed to think that when lending to governments the well-tried maxims of sound banking could be put aside. When the World Bank was negotiating a very complicated loan package to a particular under-developed country, a well-known American banker got on the first available plane and offered the same amount with no conditions attached whatsoever.

Thus on many occasions bankers failed to establish what

exactly the money was to finance, whether it was for a specific project that would in due course have an economic value or whether it was to buttress a weak balance of payments or even, to be wasted on armaments. Often no enquiry was made whether the borrower really required a loan or whether risk capital would be more suitable. Nor was any adjustment made for the foolish discrimination against foreign capital practised by many less developed countries. In effect these borrowers were given a blank cheque. Money was literally pushed on them by people who should have known better. In fact if the less developed countries had received sound banking advice they would not have entered into commitments which they could never be in a position to discharge. The debtor countries provided no security other than their own guarantees. And today they resemble badly financed corporations—all debt and no equity.

International bankers also neglected to find out whether the debtor was creditworthy, allowing governments to claim that it was unreasonable for sovereign states to provide details of export earnings and import costs, of reserves of convertible currencies and of other borrowing commitments. Had these essential statistics been on bankers' desks, perhaps they would have realised more clearly that they were vulnerable to a fatal combination—sharply rising interest rates, which became an enormous burden, and deflation, which meant that the borrower's trade balance deteriorated sharply.

As for bankers' own balance sheets, in that regard, too, the old maxims were neglected. OPEC deposits placed with the banks of the Western industrial nations were short-term; these funds were on-lent at medium or long-term to third world governments. Bankers wrongly believed that floating rate loans protected them; in fact this device could only rectify a mismatch between the interest rates they had to pay and what they charged provided everything else was going as planned. It provided no guarantee that the world banking system would carry the sheer volume of credits involved when many of the loans became unsound. Central bank supervisors were similarly gulled, for nothing in their academic training had prepared them for what they actually confronted.

On 12th August, 1982, the music suddenly stopped. For on that day Mexico told the American government that she could no longer meet payments on her external debt. Western governments, the International Monetary Fund, central banks and leading banks cobbled together a rescue package which, with refinements, has been the pattern for every subsequent case. We can now see that the Western reaction was a classic 'papering over cracks'. The technique is that the IMF and the debtor country first reach agreement on a programme of economic retrenchment designed to secure substantial improvements in balance of payments performance.

This involves setting a range of economic and monetary targets for a number of years ahead. At the same time the IMF supports the programme with medium term loans. And the commercial banks are invited to agree a rescheduling of their loans and, most important, at the same time to put up fresh cash. The fatal flaw in this method is that the intensity of deflation required to secure the necessary balance of payments surpluses to pay off external debts is unrealistically severe. In fact Mexico has been the only success, largely because unique among debtor nations it has the benefits of both a strong government and an oil surplus. For the other major debtor countries, nothing has changed except that they have been given time to do what little they can.

In addition any method whereby one bank is rescued while others are allowed to go to the wall could be almost considered a fraudulent preference and even attacked as such in the Courts. Can there be a justification for using taxpayers money to bail out one set of shareholders or one incompetent management team as against another?

The overall problem today is much more serious than it was in August, 1982. I have long argued that the oil price is far too high and that in a decline a whole new set of problems would arise. The spectre of default is visible on all sides. Those who have caused the crisis must stand aside; they cannot solve the problems they have created. A new initiative providing both money and 'human resources' is essential.

THE SALOMON PLAN

My solution is on the same grand scale as Marshall Aid, which rescued a whole continent from penury. It will require agreement between the governments, central banks and commercial banks of the Western nations and must be on a totally *international* scale. Any attempts to solve the problem on a purely national basis are doomed to failure. Some of those politicians, officials and bankers who have failed to solve the problem may have to step aside. Arthur Burns, when Chairman of the Federal Reserve, is supposed to have been asked by some anxious bankers whether the Fed would rescue them if they got into difficulties. 'I will discuss that matter with your successors' was the curt reply.

The main difference between my proposals and Marshall Aid is that the latter was squandered in some countries on social experiments, (e.g. Great Britain) whilst in others (e.g. West Germany) it was used to rebuild industry. Britain's mistake should not be made again.

In formulating my proposals, I have gone to the causes of the present crisis rather than merely trying to alleviate the effects. This is the only way to make a fundamental change.

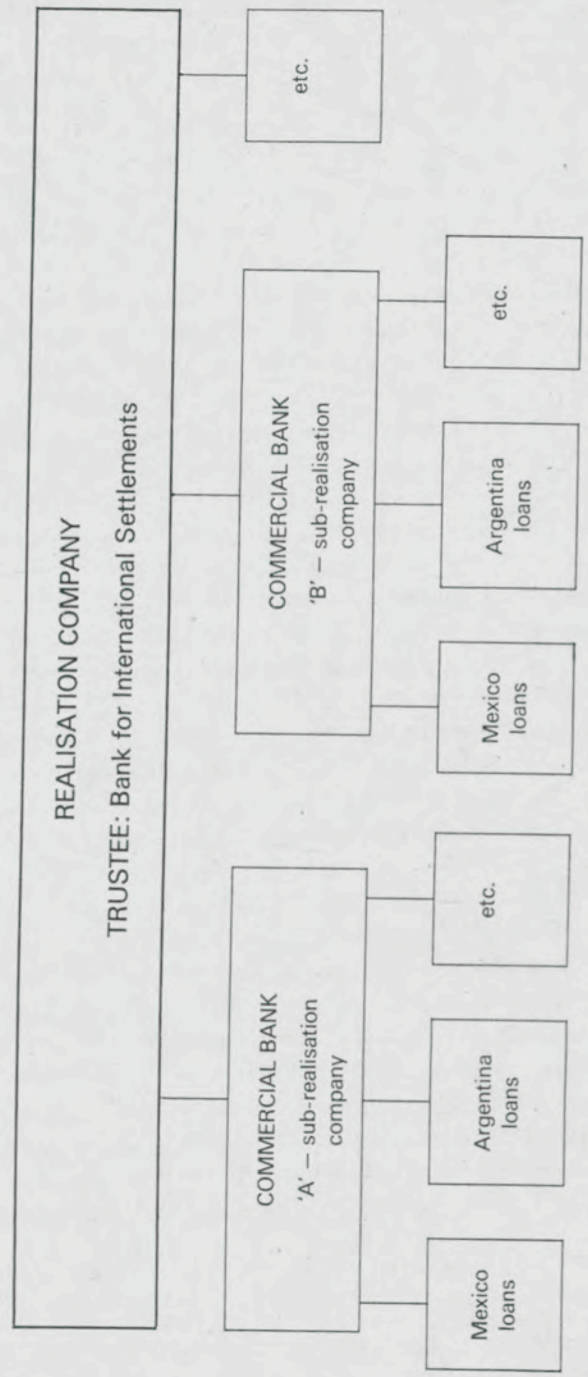
My proposals are:

1. An International Realisation Company should be set up which would have the support of all the Western central banks.
2. It would act rather like a liquidator of a commercial business by reorganising and repackaging any viable available assets, (i.e. loans) for realisation on a commercial basis.
3. It would be managed under the trusteeship of the Bank for International Settlements.
4. All non-performing loans should be taken over from the commercial banks into the temporary stewardship of the Realisation Company.
5. The Realisation Company would be empowered to re-negotiate any such loans to get them onto a sound basis by

which capital and interest can reasonably be expected to be repaid on time.

6. Legislation should be passed in all the relevant parliaments providing special tax credits enabling interest rates on non-performing loans to be reduced and/or sinking funds to be set up. The only proviso would be that all the tax saved should be used to benefit the debtor nations rather than being available to the banks. Sinking funds would be designed to repay loans within a fixed period (say 20-25 years) and interest rates should be drastically reduced—maybe by up to 50 per cent. As a *quid pro quo* for such a reduction, the Realisation Company would require that security such as oil leases, royalty agreements or shares in industrial or commercial undertakings should be provided.
7. The aim of the Realisation Company would be to sell or realise the loans on behalf of the banks as quickly as possible. This may be done singly or in packages, where possible, after renegotiation with the debtors as described above.
8. The Realisation Company would have many sub-realisation companies, each representing the non-performing loan portfolio of a particular commercial bank (see diagram).
9. It would be empowered to repackage loans—for example taking the loan exposure to one country of several banks and amalgamating them into one saleable loan. These loans would be made available on a totally open-market basis to the highest bidder. Many may only yield a fraction of their book value but others, especially if renegotiated to provide proper collateral, may come much nearer to par value and could even conceivably be taken back onto the books of the original lenders. It may also be useful to index loans either in terms of commodity prices or of inflation in the West.
10. Once a partial or whole package of loans from a particular bank had been realised, the Realisation Company would be empowered to make a repayment to the bank concerned, after deducting its expenses. In the cases of banks where lending policy has been reasonably sound, such a dividend could easily amount to close on 100 per cent. of book value and confidence in that bank's balance sheet would quickly be restored.

PROPOSED STRUCTURE OF REALISATION COMPANY



11. The debtor nations would also have to sell assets to se[rvice] some of their borrowing commitments. These assets could take the form of oil leases, natural resources operations or shares in industrial or commercial undertakings at present in government control.

12. Some banks, however, would have to accept that much if not all of their capital had been lost and shareholders would have to be prepared to supply new capital for reconstruction, allow other investors to make good the balance sheet or, if neither of these are possible, agree that weak units should be merged with stronger banking institutions.

13. The accounting treatment of any non-performing loans under the stewardship of the Realisation Company in the books of the commercial banks would have to be very closely monitored by the banking supervisory authorities. It would be wrong to say that in every case loans should be totally written off but equally a conservative approach should be taken so that banks are unable to continue to bolster their balance sheets with worthless loans.

14. The Realisation Company would be granted immunity from any litigation from any third party as a result of its stewardship of non-performing loans.

Once confidence has been restored to the world banking system by this method, it will be necessary to agree the following future practice:

1. Less developed countries would have to agree that in return for new borrowings, they would waive restrictions preventing foreigners taking a charge over assets situated within national boundaries. Future borrowings should be on a fully secured basis. These countries should also allow foreign equity capital to play a role in their development.

2. Central banks and other supervisory authorities would have to insist more explicitly than hitherto that banks keep their international lending within prudent limits. Governments would also have to ensure that supervisory bodies had sufficient powers and were adequately staffed with experienced bankers.

3. Where governments want commercial banks to make available credits to particular countries for reasons of national interest, then governments should guarantee these loans. In other words, bank lending for the risk of shareholders should be carried out only on the strictest commercial criteria.

4. Stringent conditions should be placed on what loans are used for, in particular that they are not used to purchase armaments.

Let me explain these principles in some detail.

It is not widely known that the Accepting Houses Committee in London came into existence in similar circumstances as I am proposing for the new International Realisation Company. In 1914, a standstill agreement was reached, and the merchant banks formed themselves into a Committee at the onset of World War I.

At present the big debtor countries are caught in a vicious circle. However large is the surplus that they earn on trade, high interest charges on their existing debt often amounts to an even greater figure. The result is that a certain amount of interest each year must be capitalised and added to the debt total. So the following year there is an even higher interest bill to meet and so on.

Brazil provides a perfect example. Its external debt now totals some $100 bn. The annual interest costs are therefore $11 bn, or perhaps more. Brazil's expected surplus on visible trade this year will easily be an all-time record and almost twice that achieved in 1983. But even so, the projected trade surplus—co-incidentally also $11 bn—would be entirely taken in interest payments, leaving nothing over for imports of services or repayment of principal. Brazil's external debt total, therefore, would still rise.

It is in this context that my suggestions of lowering the effective interest rate and encouraging the release of assets by less developed countries should be seen: acted upon together they would result in a reduction of indebtedness and then a lower interest charge, and so on.

Both principles will no doubt meet strenuous opposition. Many people within the less developed countries see foreign ownership as an infringement of sovereignty and as a licence for exploitation, remembering as they do earlier eras when foreign interests did perhaps sometimes take too much for themselves. But I am not proposing that, say, the entire Mato Grosso should be given to foreign bankers. What I foresee is that they would be offered shares (not necessarily constituting majority control) in productive enterprise as settlement of particular debts. Such shares could then be sold by the banks to industrial and commercial companies that could make a real contribution to the country's development; each transaction being approved by the host government. Britain herself, for instance, has felt able to allow a large number of foreign companies to participate in the development of North Sea Oil without arousing popular fears about foreign control of a valuable national asset.

Equally, many people in the industrialised West will vehemently object to any tax concessions that would ease the debt crisis. They would fear that this would be costly to tax payers, that it would in some way bail out the commercial banks and that it would represent a free gift to undeserving third world nations which have badly managed their economies. I must emphasise that my proposed tax rebate would go back entirely to the debtor countries and not to the banks. And I suggest that tax payers as a whole would benefit to a much greater extent from the increased trade opportunities that an end to the debt crisis would bring.

In any case, it is only when the debtor countries can be seen to be reducing their external obligations that conditions will be suitable for tackling the difficult problem of the solvency of the commercial banks. My solution is based upon the fact that in sophisticated financial markets such as the Western nations possess there is indeed a price for everything. In particular there would be buyers of the banks' loans to the major debtor countries. Assuming that the terms were attractive the purchasers would either be commercial companies doing business with the countries concerned, where settling a loan commitment could be part of a commercial bargain, or long term investors. This latter group has always been prepared to evaluate foreign debt risks, as the flourishing market after 1945 in the foreign bonds of countries affected by the war testifies. What is needed is some way of packaging and displaying the banks' non-performing loans so that both these classes of purchaser may come forward.

That is why I propose an International Realisation Company. It would in effect be a sales agency for the bank creditors, with the job of listing, categorising and re-arranging non-performing loans

into saleable packages. It would also, with the Bank for International Settlements as its trustee, take the lead in re-negotiating more appropriate loan terms with the debtor countries.

Once a market in non-performing loans had been established, it would finally be clear exactly what damage to their balance sheets the commercial bank creditors had sustained. The central banks and banking supervision authorities would be able to assess with a fair degree of accuracy what further write-offs banks would need to make.

I have no doubt that results would be mixed. Some leading banks would emerge from the ordeal reasonably intact. A conventional capital raising exercise would make good any short-fall. Such banks would carry on in their present form. Other famous names would be less happily placed. Some would find that they had lost most or perhaps all of their capital. When it is remembered that leading international banks have generally built up balance sheet totals to 20 times or so their capital and reserves, this is not surprising. Any bank with more than seven or eight per cent of its loan book classified as 'non-performing' has put its entire capital at risk.

There would be no advantage to any particular bank in refusing to join in the scheme as the relevant regulatory authority would examine its books very closely indeed and disregard any doubtful loans in calculating its capital ratios for solvency purposes.

One of the Chairmen of the U.K. clearing banks as recently as 31st July, 1984, was reported as dismissing a secondary market in non-performing loans. He is quoted as saying 'It's not an area in which we have any experience nor do we intend to acquire any'. As the *London Standard* pointed out:

> 'That is the sort of remark which could look silly indeed in a year or two. Imagine the chairman of a bank making the same comment about a secondary market in British Government debt. How we'd all laugh.
>
> But unless or until a serious secondary market in dud loans develops, we shall find it hard to believe in the banks' provisions against them. And where investors don't believe, they knock the share price down accordingly.'

I foresee that badly affected banks would have to be reconstructed. They would be most conveniently divided into an 'old' bank, comprising only the non-performing loans being managed by the International Realisation Company, and a 'new' bank carrying on the rest of the business. The 'old' bank which existing shareholders would own, would in effect be in receivership and its shares would be worth very little if anything. The 'new' bank would require fresh capital. This could be supplied either by the 'old' bank shareholders or by new investors. 'Old' shareholders may be given preferential rights or options that would facilitate their participation in the 'new' bank.

CONCLUSION

How do we avoid all the same old mistakes being made again? I am afraid that as far as many large banks are concerned, burnt fingers are not sufficient warning. For the banks which a decade ago discovered they had lent far too much for property development were five years ago embarrassed by imprudent lending to oil tanker owners and today rue their involvement with Latin America. For this reason I propose some institutional changes.

Lending to sovereign governments and their agencies should be secured by charges on assets in the same way as conventional lending. The precedent has already been set by the Bank for International Settlements which has successfully demanded security (often gold bullion) when making bridging loans to countries engaged in negotiating a medium term credit with the International Monetary Fund.

However, less developed countries should go further than providing security for loans. They should admit foreign equity capital into their development projects in order to provide balanced financing. Such capital could be attracted on terms that would satisfy international investors without damaging national sovereignty or interests. In fact, if this had been a feature of less developed country investment over the past fifteen years, there would be no debt crisis. Equity capital would have performed its historic role of providing a reserve or cushion during hard times.

Banking supervision should be taken out of the hands of the civil servants and fonctionaires who run the central banks. The canons of sound banking are well known and have stood the test of time in many countries. They should form the rules under which banks work. But it is very important that supervision is carried out by people who understand banking rather than by officials who know only government. In London it would not be difficult to imagine an independent supervisory body set up by bankers for bankers which would do the job much better than the Bank of England.

Finally, there remains the sensitive issues of timing and confidence. I have written this paper to stimulate discussion of the dangerous situation we are facing; moreover, I think it is particularly important that the voices of those who bear no responsibility for the present crisis are heard. Yet if the public at large should come to believe as discussions dragged on that the problems were insoluable, confidence in the financial system itself would be shattered. Well-meaning people could bring about the very situation they are trying to avoid.

When a critical mass of support has been achieved, it will be time to talk to the parties involved in the crisis. It may then be possible to see whether the necessary great international consensus involving the World Bank, many national parliaments, the central banks and the world's great commercial banks can be effected. It will need a monumental effort of will from all those concerned and a great deal of cutting through red tape but success would be a prize the value of which we can hardly contemplate.

APPENDICES

BONDS FOR THE ARAB OIL FUNDS

(An article which appeared simultaneously in The Times*, London, and* Die Welt*, West Germany, on 29th January, 1975.)*

The free world's industrial and monetary system is still reeling under the shock of the huge increase in oil prices since October, 1973, which has contributed to recession in industrial activity, to unemployment, to inflation in prices, and to balance of payments problems of vast magnitude.

The strangulation of the up to now powerful industrial nations increases the tendency to war for there is a danger that the oil exporting countries by overplaying their newly gained power will create unstable and untenable geo-political pressures. In this context the sacrifice of Israel as the price for further goodwill is not a solution or even necessarily relevant to oil pricing policy which in any case involves nations other than the Middle East. At the same time it is said (in the Neue Zürcher Zeitung of 24th December, 1974) that the Israelis have the know-how of nuclear weapons and it would be too dreadful to contemplate that in despair they might be tempted to use them. Past experience has shown, particularly in Europe as in the case of Czechoslovakia in the 30's, that long-term objectives cannot be achieved at the expense of other countries.

For the majority of the oil exporting countries a continuation of the developments of the last few months is also undesirable. On the contrary, they are interested in the stability of the monetary systems of the western world. They consider themselves, at least as far as the countries with non-marxist Governments are concerned, as economically integrated with the West.

At the same time one must remember that the oil cartel cannot last for ever and that market forces will produce an adjustment in the long run. Alternative sources of energy will become increasingly important and a relative reduction in crude oil prices is inevitable; in the light of this the oil producing countries have an interest in making provision for the 'lean' years to come in which they can finance with their present earnings their further economic diversification and development.

The solution which has to be found, therefore, is one which will:

(a) enable the economies of the oil importing countries to absorb, and adjust to, the large increase in price of one of their basic raw materials in a way which does not lead to economic and political instability through levels of inflation or unemployment which are found intolerable.

(b) enable the financial mechanisms of the free world to continue to function smoothly by removing the instability caused by huge amounts of petro-dollars swilling around the short-term money markets and representing short-term obligations which cannot be met.

(c) give the oil-exporting countries a claim (on real resources) over a long period of time (when the adjustments in the importing countries have been made) when alternative sources of fuel have been developed, when oil prices fall or when their reserves have become much reduced or depleted and when they are able to absorb their increased revenues—without inflation—through development of their own infra-structure, an increase of population and their standards of living.

The proposal which would meet all these objectives (and which are not met by the present Kissinger/Healey plans because the total amounts are too small and because they merely postpone the crunch for a short period), are as follows:

1. The oil importing countries would pay for their oil, in cash, the same prices (with some adjustment for inflation) as those ruling prior to the October 1973 war in the Middle East.

2. The difference between those prices and those now current would be paid in 25 years bonds.
3. The trusteeship of these bonds will lie with the Bank for International Settlements which is an independent banking organisation and has the experience of the Dawes and Young Loans to draw upon.
4. The B.I.S. will clearly define and limit the tranches of the individual debtor countries—with an overall limit of $300 billion.
5. These bonds will be inflation indexed in accordance with some agreed units of measurement and in order to protect the oil-exporting countries against the erosion of the value of money. In view of this, however, they would carry an interest rate of only 3½% per annum.
6. The oil exporting countries will be able to tender these bonds in payment against the import of goods and services from the oil-importing countries, but not in payment against the acquisition of assets.
7. The bonds will carry a sinking fund.

Arrangements of this nature meet all the requirements laid down in points (a)-(c) above. In a minor and modified form they have already been adopted by Venezuela which has reached agreement with Costa Rica, El Salvador, Gutaemala, Honduras, Nicaragua and Panama under which these countries receive their oil at market prices ($11·90 a barrel) but $6 a barrel will be handed back as a five-year loan at 8 per cent.

The proposals now outlined are, of course, only those of principle; the details and refinements will have to be worked out by negotiations.

ORIGIN AND CURE OF THE INTERNATIONAL BANKING CRISIS

(An article published at the Annual General Meeting of Rea Brothers Plc on 14th April, 1983.)

Central Banks

To a great extent the origin of this banking crisis stems from the fact that years ago the central banks which were in the hands of the market (private enterprise) were nationalised.

When the central banks were in the hands of the market their decisions were founded on commercial considerations based on prudence and foresight. When the State became the owner it could direct the central banks to act in a manner which was totally inconsistent with these principles.

Political considerations played an enormous part and the state (the politicians) at times adopted measures in order to buy the favour of the public for electioneering or other purposes. I said many years ago that in the old days the politicians were accused of buying votes with their own money and in modern times they are being accused of buying them with the taxpayers' money. At the time I posed the question might it not be better to go back to the old system?

We have to realise that in modern times we cannot put the clock back so a denationalisation of the central banks is not within the realms of possibility. However, what is a possibility is that certain safeguards are introduced to prevent reckless and unwise measures based purely on national or international politics.

The central banks could be brought under the control of a totally independent body outside government, and I referred to this in an article which was published in *The Spectator* in 1967 under the heading 'Bankers of the World Unite!'. Alternatively, a separate international central bank would be formed which would be in the hands of the market.

Non-Performing Loans

The present crisis is based on the fact that central banks or other monetary public institutions have encouraged, or if not actively encouraged, have not controlled the international banks in lending money to unworthy debtors; the old principles of sound banking were totally disregarded because many of the loan officers who had to decide about these credits, whilst they might have learned which tools to use, did not learn how to use them.

The extent of the present crisis is shown by the article reproduced on pp. 32-33. It appeared in *The New York Times* on 18th March, 1983 and I have decided to include the full text herewith.

With the decline of the impact of the owner-occupier, as far as the funds of the banks were concerned, ambitious people wanted to compete with other ambitious people.

One of the maxims of a good banker is that if he lends money he will apply a number of different criteria:

(i) if someone wants a loan the banker will first make quite sure that the debtor really needs a loan and that it is not really capital he requires;

(ii) if the banker comes to the conclusion that the former is true then he must find out whether the debtor is credit-worthy;

(iii) once he finds out that the debtor is credit-worthy he must find out whether the cash flow will be sufficient to enable the debtor to fulfil the terms of his loan agreement;

and last but not least:

(iv) if the credit is to be given to a debtor in another country, the banker has to be entirely satisfied that the balance of payments of that country will suffice to cover the terms of the agreement.

But this is only the beginning of the terms at which the banker should look. The following are also of great importance when a banker gives credit:

(i) the size of the total credits he is giving in relation to his capital reserves;

(ii) he should not give one debtor more than a certain percentage of the credit he is willing to give altogether;

(iii) if in trade, or commodities, or industry, the credit should as well be limited in size to a specific percentage of the trade or commodity or industry being financed;

(iv) if it is to foreign countries, again it should be limited to a percentage of the total funds available.

We are at present in the position that many of the leading banks have infringed all or part of these criteria and they now find that a great amount of their capital and reserves is locked up in what are today being called 'non-performing loans'. If this were to happen to a small bank and their funds were locked up in such a manner, the authorities would immediately come and demand the writing off of these loans or the transfer to reserves of sufficient funds to cover them, and would not allow the banks to go beyond that, and here I refer to the new banking supervision, i.e. the agreed ratio on which banks can lend money in relation to their capital and reserves.

We have now the extraordinary position where some of the central banks are actively encouraging their commercial banks to add to the loans already given to non-performing debtors—that means throwing good money after bad—to prevent non-performing debtors from failing in their interest payments. In other words, the new money lent is being added to the already outstanding loans and is being used to meet the interest payments.

One of the basic banking principles is that it is almost a criminal offence to borrow short and to lend long. This is another reason for the present banking crisis. The Governor of the Bank of England said in a recent speech (7th February, 1983):

> 'The foreign branches of banks from some countries in difficulty had taken very substantial short-term deposits from other banks and largely lent them back at longer term to their home countries. These short-term deposits were so large that any significant withdrawal of them would have jeopardised the whole package of support facilities. Moreover, if some banks succeeded in reducing their exposure, others would be strongly tempted to follow suit.'

Finance to Under-Developed Countries

The huge balances which the OPEC countries had with the

international banks have been disappearing, or are about to do so. These balances were more or less all on short term, but were used on a much longer term basis in order to finance the under-developed countries; not necessarily for building up their infrastructure but also for financing their countries' budget deficits. Now these countries cannot pay back the money and the banks have had to find the money to repay the balances owed to the OPEC countries.

I well remember my old friend, George Woods, who was the first President of the World Bank, telling me the terms and conditions on which the World Bank would lend money and he said the loan always had to be for a specific project, well documented and properly supervised. We have come a long way since then and money is often neither lent for specific purposes nor is it well supervised.

One of the results of this is that many countries borrow far too much and do not allow sufficient capital to back up these loans so there is not sufficient ratio between capital and loans. This has arisen because, for nationalistic reasons, countries have been refusing to allow foreigners to participate on the capital side. They discriminate against capital participants by special laws or special taxes.

The present crisis is very often compared with what happened in 1929 when people jumped out of windows because they could not fulfil their commitments. That crisis was small fry compared with what we are facing today and, in fact, the real crisis then only made its full impact in 1932 when against an index of 372 on 24th October, 1929 ('Black Thursday'), or 224 on 13th November, 1929 (the lowest point at that stage) the New York Industrial Average slowly fell to a mere 58 in 1932 (July 8th).

However, the situation at that time was different because even if people had sold their investments in time a great number of the banks in which they deposited their funds failed and they lost their money that way.

The powers that be are today well aware of this and feel that if they were to allow one of the big banks to fail the domino principle would apply. This might well be and I am all for preventing it, but at present I cannot see any necessary measures being taken to do so.

THE TOP 10 U.S. BANKS AND THEIR LOAN EXPOSURE IN THE THIRD WORLD

Bank holding companies ranked by 1982 total assets, all data as of year-end 1982.

	MEXICO		BRAZIL		VENEZUELA		OTHERS*		TOTAL		
	Loans ($ mill.)	% of Tot. Loans	Loans ($ mill.)	% of Tot. Loans	Loans ($ mill.)	% of Tot. Loans	Loans ($ mill.)	% of Tot. Loans	Loans ($ mill.)	% of Tot. Loans	% of Tot. Equity
Citicorp**	3,270	3.8	4,360	5.1	1,090	1.3	1,090	1.3	9,810	11.4	203
Bank America	2,500	3.4	2,300	3.1	2,000	2.7	0	0	6,800	9.2	148
Chase Manhattan§	1,867	3.1	2,362	4.3	1,012	1.8	1,012	1.8	6,073	11.0	220
Man. Hanover	1,730	4.1	2,014	4.7	1,100	2.6	1,967	4.6	6,811	16.0	245
Morgan Guaranty	1,082	3.4	1,688	5.3	543	1.7	759	2.4	4,072	12.8	150
Chemical	1,500	4.9	1,300	4.2	0	0	741	2.4	3,541	11.5	182
Continental Illinois	695	2.1	490	1.5	463	1.4	381	1.2	2,029	6.2	119
First Interstate	680	2.8	474	1.9	0	0	0	0	1,154	4.7	64
Bankers Trust	875	4.2	875	4.2	475	2.3	0	0	2,225	10.6	143
Security Pacific	525	2.1	490	2.0	0	0	175	0.1	1,190	4.8	80
TOP 10 TOTAL	14,544	3.4	16,353	3.9	6,683	1.6	6,125	1.4	43,705	10.3	169

* Includes disclosed exposures of more than 1 per cent to Argentina, Yugoslavia and Chile.

** Loan amounts calculated from a percentage of total outstanding.

§ Loan amounts calculated from a percentage of total outstanding, and the midpoint of the range for each country is listed. Range for Argentina and Venezuela is $675 million to $1.35 billion; for Mexico $1.35 billion to $2.025 billion; and for Brazil $2.025 billion to $2.7 billion.

Source: The American Banker

The nation's 10 largest banking companies had $43.7 billion at risk to financially troubled developing countries at the end of 1982, more than half again the value of their equity, according to figures contained in their recently released annual reports.

That means if none of those loans and investments were repaid, the investments of the banks' shareholders would be wiped out and the banks would not be able to repay all their creditors.

The likelihood of that happening is considered zero by most bankers and bank analysts. Even when a company goes bankrupt, a bank usually gets back at least a third of what it lent.

But some analysts say that the high levels of loans to the troubled countries could mean that the banks eventually will have to raise additional capital at prices well below their nominal book values.

'Day of Reckoning'

'A large portion of these banks' equity capital is effectively tied up or frozen in these various countries,' said Thomas H. Hanley, a vice president and bank analyst of Salomon Brothers. Another analyst, who asked not to be named, said, 'There's a day of reckoning coming when a number of these big banks will have to sell equity capital at punitive prices.'

For their part, however, the bankers contend that they expect to lose very little of their outstanding loans to the troubled nations. These include Mexico, to which the 10 banks lent $14.54 billion; Brazil, $16.35 billion; Venezuela, $6.68 billion; and Argentina, Yugoslavia and Chile combined, $6.13 billion. The exposure of the 10 banks to these countries represented 169 per cent of the banks' equity.

'The chance of losing all these loans is almost non-existent,' said Francis X. Stankard, executive vice president of the Chase Manhattan Bank.

According to figures compiled by the American Banker, *a trade publication, Chase's exposure to Mexico amounted to $1.7 billion, to Brazil, $2.4 billion, Venezuela, $1 billion, and to Argentina, Yugoslavia and Chile, $1 billion. These outstanding loans represented 220 per cent of the bank's equity.*

In relation to its equity, Chase's exposure was the second highest, following the Manufacturers Hanover Trust Company, which had 245 per cent of its equity invested in the troubled countries.

Some bankers questioned the value of the information, which they were required to disclose by the Securities and Exchange Commission. One problem, they said, was that S.E.C. did not clearly define what it wanted and therefore the figures and ratios are not comparable.

Another problem, they said, was that the figures do not include local currency loans made within the foreign countries by branches and subsidiaries of American banks. For example, 40 per cent of Citicorp's earnings from Brazil were from loans made within that country and therefore not included in the report of its Brazillian exposure.

One New York banker, who asked not to be identified, said 'There are no surprises in these numbers. What is surprising is the relative standing.'

Among the top 10, two California banks had the least exposure in terms of equity. They were the First Interstate Corporation, with exposure to the troubled countries representing only 64 per cent of its equity, and the Security Pacific Corporation, with 80 per cent.

An article by Robert A. Bennett which appeared in the *New York Times* on 18 March 1983.

I have read statements in the newspapers by leading personalities saying that the banking crisis is over, that things are under control, etc. etc. It is an attitude of hoping that something will happen to save the situation, and sweeping the dirt under the carpet. I regard this as a very dangerous attitude to adopt and the longer one waits before dealing with the problems in a practical manner the worse the situation will become—I have already pointed out how severe things will be. It may well be that the Russians can safely agree to a reduction in their nuclear armaments and rely on what Lenin once said 'There is no need to worry about capitalism; it will destroy itself through the disintegration of the monetary system.'

Proposed Cure

Now what is the solution?

(i) to prevent governments (politicians) from dealing recklessly with the powers vested in them by virtue of their controlling the central banks, and

(ii) by the commercial banks subjecting themselves voluntarily to the disciplines to which I have already referred. However, before we can come to this we have to straighten out the balance sheet of the banks so that the non-performing loans cannot be counted as assets in considering a loan policy, or rather the relation of capital reserves to the loans they gave. I will refer to this again later.

A very imaginative initiative has to be thought of; something on a very grand scale of the kind which General Marshall introduced at the time with his Marshall Aid Plan, except that this aid should be confined to a very specific purpose. In the original Marshall Plan the disposition of the money was left to the countries which received it. Some, like Germany, used it wisely, rebuilding their industry and trade; some, like Great Britain, used it unwisely, squandering it on social experiments and benefits.

For example an international bank could be started, sponsored by the people and not in the hands of government—and here I would remind you of what happened in Genoa in the 15th century. As a consequence of that city's escapades, the economy of Genoa collapsed in 1405, and many government creditors amalgamated

to form the independent Banco di San Giorgio and save the state by taking over the national debt. In that particular case, however, the bank apparently acquired so many privileges for itself that its power soon rivalled the state itself. This mistake should not be made again.

If an international central bank of the kind to which I have referred, were started by the citizens based on private enterprise, with subscriptions from the public, to the exclusion of politicans—and I do not think this is the time or the place to go into the constitution of this bank—and if (as in the Federal Reserve System of the United States) any bank in the world could become a party to this bank, abiding by the rules and regulations laid down and incorporating the wise and sound principles of banking, then this bank, which could be set up not only in one place but also regionally, could be the lender of last resort. It is for this purpose that the new 'Marshall Aid Plan' should be provided.

As I have already said, non-performing loans which are at present the greatest threat to the international financial system, should all be handed over to a realisation company, managed and controlled by the new international central bank. The capitals of the banks which have, therefore, been denuded of these 'assets' should be replenished by financing facilities from the international central bank and from the public. A condition of this kind of initiative would, of course, be that the commercial banks would abide strictly by and become party to the rules and regulations as laid down by the international central bank, and subject themselves to proper banking supervision in this respect. Should they fail to comply they would be thrown out of the club, which would really mean the end of that particular bank as they would lose all their deposits.

It is, of course, not possible in a short article like this to go into the pros and cons of my suggestions in great depth, but I would suggest that, with great urgency, a committee of real bankers, to the exclusion of those who have contributed to the present debacle, be set up empowered to make a considered report, this committee to have the right to add to its members whomsoever they chose and the banks that wanted to participate finally would have to be very co-operative in providing information to this committee to enable it to make its report.

Conclusion

Now I do not claim that my suggestions are necessarily fool-proof but they are at least a constructive idea on how to solve a problem which, if it is not tackled in a practical and pragmatic way, will lead to a major disaster in the world. New ideas are always attacked as unworkable, cannot be done, etc. etc. Let those come forward who have constructive ideas on how to improve upon the suggestions contained in this article, or show where, for practical reasons, they should be altered.

I have had over many years quite a good track record with the comments which I have made on the economic front.

The crisis which we are now facing was absolutely foreseeable and should have been dealt with a long time ago.

As far as international loans are concerned, I only want to quote from a speech which I made in 1976 when I said:

> 'It is my firm conviction that after facing the traumatic experiences in the financial world a year or two ago, the free world is facing yet another serious crisis. I refer to the international loans which have been given to the developing countries, in many cases without any control and very often for political reasons, and then unloaded in part, to the public, and part kept in the loan portfolios of many of the great international banks. I can foresee the day, if it is not already here, when many of these countries will not be able either to service the loans or make the repayments on the due date; it is quite possible that they will argue that it was, in any case, money owed to them by the free world for what it did to them in the past or, to put it another way, for what it did not do for them in the past, and they will simply say "we owe you nothing". This is propaganda which would be encouraged by the Eastern Bloc and would help further in the ultimate goal to destroy the free world.'

Let's not sit back and throw up our hands in despair. Let's rather remember the old saying by Goethe: 'despite adverse forces, to survive, never to bend and always to walk erect, brings the support of God'.