EUROPEAN UNION AND THE DEVELOPING NATIONS' EXTERNAL DEBT: EU–15's Debt Policy, 1960–2008

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Abstract

This Master's Thesis defines the debt policy of the current European Union Member States towards the developing nations. Since no official policy for debt exists in the EU, it is defined to include debt practices (loans and debt relief in development cooperation) and debt within the EU development policy framework. This study (1) describes how the issue of external debt appears in the development policy framework, (2) compares EU Member States' given loans and debt relief to grants for the developing nations (1960s to the 2000s), and (3) measures the current orientation in ODA of each EU Member State between grant aid and loan aid using the Grant-Loan Index (GLI). Theoretical aspects include reasons for selecting between loans (Bouchet 1987) and grants (Odedokun 2004, O'Brien and Williams 2007), policy context of the EU (Van Reisen 2007) and the meaning of external debt in the set-up between the North and the South. In terms of history, the events and impact of the colonial period (where loans have originated) are overviewed and compared in light of today's policies. Development assistance statistics are derived from the OECD DAC statistics portal and EU development policy framework documents from the EU portal. Methodologically, the structure of this study is from policy analysis (Barrien 1999, Hill 2008, Berndtson 2008), but it has been modified to fit the needs of studying a non-official policy. EU Member States are divided into three groups by Carbone (2007a); the Big-3, Northern and Southern donors, based on common development assistance characteristics. The Grant-Loan Index is used to compare Carbone's model, which measures quality of aid, to the GLI measuring the structure of aid. Results indicate that EU-15 countries (active in debt practices) differ in terms of timing, stability and equality of debt practices in the long-term (1960s to the 2000s). In terms of current practices, (2000-2008), it is noted that there lies a disparity between the actual practices and the way in which external debt is represented in the development policy framework; although debt practices form a relevant portion of total ODA practices for many EU-15 Member States, the issue itself plays a minor role in development policy documents. Carbone's group division applies well to the Grant – Loan Index's results, indicating that countries with similar development policy behaviour have similarities in debt policy behaviour, with one exception: Greece. On the basis of this study, it is concluded that EU development policy framework content in terms of external debt and debt practices are not congruent. The understanding of this disparity between the policy outline and differences in long-term practices is relevant in both; reaching the UN's Millennium Development Goals, and in the actual process of developing development aid.

Keywords

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Debt

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Tiivistelmä

Tämä Pro Gradu -työ selvittää millainen on nykyisten EU-maiden velkapolitiikka kehittyviä maita kohtaan. Tarkastelussa on nykytilanne ja pidemmän aikavälin muutos. Virallista velkapolitiikkaa ei ole linjattu EU:ssa ja se määritellään tässä tutkimuksessa erikseen EU-maiden velkatoimien (lainat ja velkahelpotukset kehitysyhteistyössä) ja kehityspolitiikan linjausten sisällön muodostamaksi kokonaisuudeksi. Tutkimuksessa selvitetään (1) miten kehitysmaiden ulkomaanvelka esiintyy EU:n nykyisen kehityspolitiikan linjauksissa, (2) vertaillaan EU-maiden eroja annetun laina-avun ja velkahelpotusten määrää lahja-apuun (1960–2008) sekä (3) muodostetaan ”Lahja-Velka Indeksi”, joka mittaa EU-maiden nykyisiä eroja kehitysavun orientaatiossa laina-avun ja lahja-avun suhteen (2000–2008). Käsitelty teoria pohjautuu lainojen (Bouchet 1987) ja lahja-avun antamisen (Odedokun 2004, O'Brien & Williams 2007) problematiikkaan, EU:n politiikkakontekstin kuvaamiseen (van Reisen 2007) ja ulkomaanvelan merkityksen analysointiin ”Pohjoisen” ja ”Etelän” välisenä haasteena. Historiaosiossa esitellään lainanannon alkuperää (Duignan & Gann 1971) ja arvioidaan siirtomaa-aikakauden tapahtumia ja niiden merkitystä nykyisessä velkapolitiikassa. Tilastollinen aineisto on OECD:n DAC:n tilastoportaalista, EU:n kehityspolitiikan linjauksia koskevat dokumentit EU:n verkkoportaalista. Tutkimuksen rakenne noudattaa policy-analyysia (Barrien 1999, Hill 2008, Berndtson 2008), mutta sitä on muokattu tukemaan epävirallisen politiikan tutkimusta. EU-maat jaetaan tarkastelussa Carbonen (2007a) mukaan ryhmiin (”3 suurta”, ”pohjoiset” ja ”eteläiset”), jotka pohjautuivat yhteneviin kehityspolitiikan piirteisiin. Lahja-Velka Indeksin avulla vertaillaan, miten Carbonen kehitysavun laatua mittaava malli suhteutuu ryhmäjaon osalta kehitysavun rakennetta mittaavan indeksin tuloksiin. Tutkimustulosten mukaan EU-15 maat (joilla velkatoimia on ollut) eroavat velkatoimien osalta pidemmällä aikavälillä ajoituksen, vakauden sekä tasapuolisuuden suhteen. Nykytoimien ja voimassa olevien kehityspolitiikan linjausten välillä todetaan vallitsevan epäsuhta; vaikka velkatoimet muodostavat merkittävän osan useiden EU-maiden kehityspoliittista toimista, niiden rooli ja osuus kehityspolitiikan linjauksissa on marginaalinen. Carbonen ryhmäjaon todetaan soveltuvan myös tähän aineistoon; pohjoiset donormaat ovat oletetusti apuorientoituneita, ”3 suurta” velka- ja apuorientoituneita ja eteläiset maat pääasiassa velkaorientoituneita, poikkeuksena Kreikka. Tutkimuksen perusteella todetaan, että EU:n velkapolitiikan linjaukset ja viralliset toimet eivät nykyisellään ole mittakaavaltaan yhteensopivia. Tämän epäsuhdan ja velkapoliittisten toimien erojen ymmärtäminen on tärkeää kehitysyhteistyön tavoitteiden saavuttamisen kannalta, sekä itse kehitysyhteistyöjärjestelmän kehittämisen näkökulmasta.

Avainsanat
Kehitysyhteistyö
EU-maat
Kehitysmaat
Politiikka
Velat
Kansainväliset suhteet
Kansainväliset tilastot

Preface

The issue of external debt of the developing nations combines many of the greatly interesting and highly important issues in development studies; international relations, colonial history, urge and desire to ”develop” and become ”developed”. Studying them in the context of the EU adds many interesting additional layers. Original plan for my Master’s Thesis was to research the economic relations between developing countries and the European Union. However, while I did initial research for that subject, I kept encountering the issue of external debt of the developing nations. When I started searching for more specific information concerning EU’s policy towards the issue, I wasn’t able to find the information I needed. From that point onwards I became more interested in the topic, and shifted my focus finally entirely on it. In discussion with experts from various fields I became more and more convinced of the relevance of this study. Due to limited previous research and complex structure of the problem, the hardest thing in this study has been to limit the topics included and items discussed.

Conducting this thesis has been a greatly enjoyable learning experience, to which many people have contributed to. My gratitude goes to my main supervisors, professor J. Koponen and M. Stocchetti. While Juhani has been a major influence in finding the right composition for this study overall, Marikki has given great direction concerning issues relating to especially the EU. Both have proposed right kind of questions which have helped in finding right kind of answers. Professor K. Vehkalahti has given me the opportunity to finish this thesis during an internship under the Department of Social Research. During this internship he has dedicated his time for guiding me, and also given great ideas especially concerning the use of SURVO and LaTeXsoftwares. I would also like to thank other faculty members, especially PhD P. Multanen and PhD J. Gould, for their open spirit in teaching. The short time period spend in your lectures has had a great influence on my life. During the past year I have participated in a mentor program of the Finnish Association of Political Scientists and I’m grateful for my mentor PhD R. Horppu, who has guided me during the past year. Thank you all for your time and patience.

Finally, I would like to thank my parents for letting me freely choose my direction in life and Visa, thank you for your endless support during the time I’ve spent studying at the University of Helsinki. You have made me laugh and find my way whenever the process of this Master’s Thesis had devoured me too deep.

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Abbreviations

ACP African, Caribbean and Pacific country group

AfDB African Development Bank

AfDF African Development Fund

AsDF Asian Development Fund

CarDB Caribbean Development Bank

CFSP Common Foreign and Security Policy

DAC Development Assistance Committee

EBRD European Bank for Reconstruction and Development

EC European Commission

EEC European Economic Community

ECB European Central Bank

ECHO European Community Humanitarian Office

ECLA United Nations Economic Commission for Latin America and the Caribbean

EDF European Development Fund

EIB European Investment Bank

EP European Parliament

EPA Economic Partnership Agreements

EU European Union

GAVI Global Alliance of Vaccines and Immunisation

GEF Global Environment Facility

GDP Gross Domestic Product

GLI Grant – Loan Index

GNI Gross National Income

HIPC Highly Indebted Poor Countries

IBRD International Bank for Reconstruction and Development

ICSID International Centre for Settlement of Investment Disputes

IDA International Development Association

IFAD International Fund for Agricultural Development

IFC International Finance Corporation

IMF International Monetary Fund

IPE International Political Economy

LDC Least Developed Countries

LIC Low–Income Countries

MDG Millennium Development Goals

MDRI Multilateral Debt Relief Initiative

ND Northern Donors

NIC Newly Industrializing Country

NGO Non–Governmental Organization

NIEO New International Economic Order

NPV Net present Value

ODA Official Development Assistance

OECD Organization for Economic Co–Operation and Development

PCD Policy Coherence for Development

PRS Poverty Reduction strategy

PRSP Poverty Reduction Strategy Paper

SAP Structural Adjustment Program

SD Southern Donors

UNAIDS Joint United Nations Programme on HIV/AIDS

UN United Nations

UNCTAD United Nations Conference on Trade and Development

UNECE United Nations Economic Commission for Europe

UNFPA United Nations Population Fund

UNHCR United Nations High Commissioner for Refugees

UNICEF United Nations Children's Fund

UNDP United Nations Development Programme

UNTA United Nations Regular Programme for Technical Assistance

WB World Bank

WFP World Food Program

WTO World Trade Organization

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Chapter 1

Introduction

"Debt is a social and ideological construct, not a simple economic fact."
–Noam Chomsky, 1999

"A country facing debt difficulties today would run into the same problems it did three decades ago, namely that there is no internationally recognized procedure to work–out sovereign debt difficulties in a fair, predictable and transparent manner."
– Eurodad, 2010

The Member States of the European Union have given Official Development Assistance ODA to the developing nations since the 1960s (OECD DAC, 2010). Collectively, The European Union is the world's largest provider of development assistance; in 2008 the EU–15 provided $70.2 billion in aid, representing 59 per cent of total OECD DAC aid (OECD Aid, 2010). In addition to giving development aid in the form of grants, EU Member States also give loans. Since the debt crisis of the 1980s, high external debt in the developing nations has been considered one of the main obstacles of development. The detrimental nature of loans to the developing nations has been known for nearly three decades, still in 2007 36.8 per cent of Africa's loan accumulation was bilateral in nature (21.84 per cent was multilateral and 41.58 per cent private)(OECD DAC, 2010). Although the European Union Member States have acted as creditors for decades and the direct link between high external debt and poor level of development is widely known, no official policy for loans to the developing nations has been created within EU's development policy.

This Master's Thesis describes and analyzes the debt policy profile of the EU and its Member States by forming the debt policy profile in three parts; (1) explaining how the issue of external debt appears in the EU development policy framework, (2) describing how EU Member States have given loans and debt relief in relation to grants to the developing nations since the 1960s to the 2000s, and (3) by measuring the orientation of ODA of each EU Member State between grant aid and loan aid for the current development era by developing a Grant – Loan Index.

1.1 Research Problem and Objective

In 2006, the overall total debt accumulation for the developing world was $2.7 trillion, and the overall annual (global) total for development assistance was $106 billion. (WB, 2010b,a) Developing nations high external debt appeared as a problem in global economics and politics in the aftermath of the debt crisis in the early 1980s. Although external debt in itself is not a problem, high amounts of it and lacking economic or political capability of a nation to handle its payments continue to be a hindrance of development. (Befekadu, 2001, Fikru and Getachew, 2008, Hippolyte, 2009)

The relationship between grants and loans in Official Development Assistance is quite complex. Numerous different kinds of types of both grants and loans have evolved, developed and appeared in the structure of ODA in OECD DAC statistics, since the 1960s (OECD DAC, 2010). In addition to the added number of different types and sectors of ODA, many agreements have been consummated between various EU Member States and the developing countries during the time period from the 1960s to the 2000s.

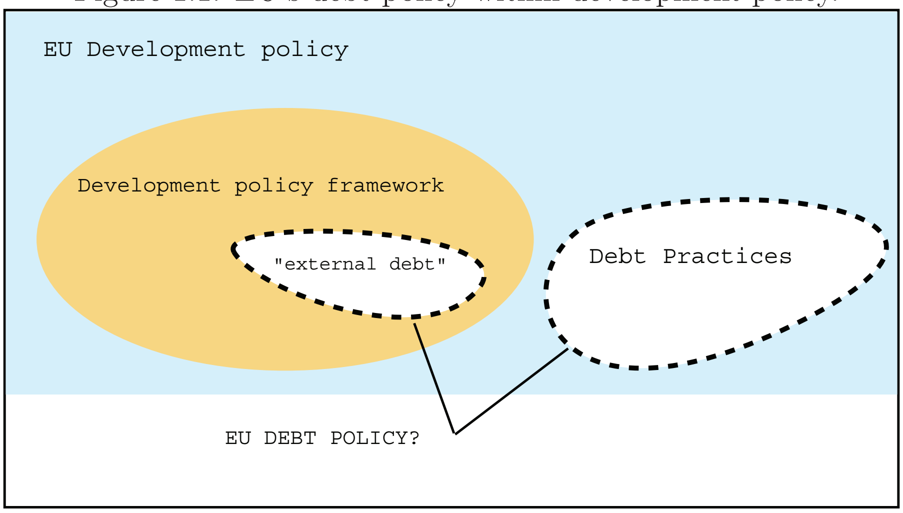
Content wise, studying the debt policy of the European Union Member States is important since the developing world still suffers from severe hindrances of development, to which high external debt has an influence on. Developing world still suffers from extreme poverty; about 1 billion people live on less than 1$ per day (Earth Institute, 2010) Income gaps in the world overall are still widening; in 2008 the World Bank announced statistics concerning the year 2005, and concluded that at least 80% of humanity lived on less than $10 a day (Global Issues, 2010) and more than 80% of world population live in countries where income differentials are still widening. (UN Human Development Report, 2009). EU is the world's largest donor and the primary goal of its development cooperation policy is poverty eradication (EU Policies 2009). Development assistance and loans within it have been given since the 1960s (OECD DAC, 2010), but no official debt policy still exists. Out of current loan accumulation, more loans are bilateral than multilateral (OECD DAC, 2010) although most often critique is directed towards the multilateral creditors, see for example Chossudovsky (1999), and George (2004). Most of development assistance research has been focused around the outcomes of given aid, not necessary the composition or structure of given aid. See for example Carbone (2007a) and Odedokun (2004).

The aim of this study is to make EU debt policy politically visible by describing first the actions in general, while also comparing them to statements concerning debt in development policy framework. EU debt policy is currently not known or present in development policy discourse, but this study changes that by forming EU debt policy profile. Making the policy "visible" and real by studying it is very important. This profile has value firstly because defining practices is the needed initial step in the lengthy process of studying the policy's larger influences. Secondly, knowledge of the differences in these actions give insight to determining the current fields of improvement. These are important when EU Member States act to reach development policy goals, such as those outlined in UN's Millennium Development Goals to which the EU Member States agreed to in 2000. Thirdly, defining the debt policy profile provides new knowledge of the EU development policy practices, which can be applied in the different fields of both EU and development studies.

1.2 Research Method and Design

The study of politics and policies have different roles in a society. The objects of study can either be decision–makers, citizens (or groups of citizens), institutions, or media, for example. Research questions can involve the actions and interactions of these actors, such as actual decisions and decision–making, (policy) practices, or communication between the different actors. (Roos, 1973, pg. 224) The research question of this study is "What is the European Union's debt policy profile?". The focus of this study is in the debt practices of the European Union and the framework of development policy, see figure 1.1. This figure presents external debt within the framework of development policy, and the debt practices as a part of the development policy in general. These practices have not been guided by an official policy, and the only way the question of external debt appears officially in the development policy of the EU is within statements in the policy framework.

Figure 1.1: EU's debt policy within development policy.



Debt practices are defined here as those items included in Official Development Assistance which are directly linked to the external debt of the developing nations. These include loans and debt relief. In this study they are compared to grants in order to provide an understanding concerning scale of practices. The key definitions used in study are explained in table 1.1.

Development policy framework is the current formation of all agreed upon issues in EU's development policy. This study analyzes and compares the statements of debt in the current development policy framework to actual practices in the field.

Table 1.1: Key concepts used in study.

Term	Definition
ODA	Official Development Assistance (ODA) is defined as flows to developing countries provided by official agencies, including state and local governments. Each transaction of which meets the following tests: i) it is administered with the promotion of the economic development and welfare of developing countries as its main objective; and ii) it is concessional in character and conveys a grant element of at least 25 per cent (OECD Glossary, 2009).
Grant aid (in ODA)	Transfers in money or in kind, for which no repayment is required. Includes grants for technical co–operation, grant–like flows, i.e., loans extended by governments or official agencies in currencies of the donor countries but repayable in recipients' currencies and transfer of resources through sales of commodities for recipients' currencies, less local currency balances used by the donor for other than development purposes. Debt relief is included in grant aid but also reported as a separate item. (OECD Glossary, 2009).
Loan aid (in ODA)	Transfers for which repayment is required. Only loans with maturities of over one year are included in DAC statistics. Data on net loans include deductions for repayments of principal (but not payment of interest) on earlier loans. (OECD Glossary, 2009)
Grant element	Mathematical assessment on the financial terms of a transaction; the difference between the face value of a loan and the present value (at a rate of discount of 10 per cent) of the service payments the borrower will make over the lifetime of the loan. Three factors determine it: interest rate, grace period and maturity. (OECD Reporting, 2009)
Sector VII (in ODA)	Sector VII "action relating to debt", includes debt forgiveness, conversions, swaps, buy–backs, rescheduling and refinancing. (OECD Reporting, 2009)

Since the framework presented is current, but debt practices data is analyzed from the 1960s to the 2000s, history and evolution of the development policy is also presented. As a result, the evolution of both of these; the debt practices and the development policy framework are overviewed. The focus of analysis mainly remains on the debt practices, which have not been coherently compared before and which provide new information. The overall content of development policy framework is already of course known, but here it will be discussed mainly from the perspective of how the issue of external debt appears in it. As such, these two parts together will form a comprehensible profile of EU's debt policy.

Focusing on the structure of development assistance in depth serves the purpose of developing more useful and better functioning development aid practices (loans, grants and debt relief) through increased knowledge of the differences among Member States. The goal is not necessarily to label EU Member States as either "good" or "bad" donors, but to identify differences and provide information needed to develop development assistance. Suffice to say, EU Member States have largely differed in the ways and methods of giving development assistance. This is both a challenge and a highly interesting factor when studying EU politics; what are the differences between donors within a Union which has agreed to common goals and ways of practicing development policy, while still leaving room for individual decision–making? Histories of relations between the different EU Member States and the developing nations differ substantially. Development policy cooperation of the EU was established in the Maastricht Treaty in 1993 (van Reisen, 2007, pg. 47). The field of development cooperation is a field of shared competence in the EU, where Member States have the power to legislate and adopt legally binding acts on their own (EU Principles, 2009). How do these differences appear in the debt practices? And what influence do these differences have on the common goals of the Union? For these reasons, the concrete actions of Member States and the commonly agreed upon policy framework of the entire Union have been separated in this study, as they are in real life in policy areas which are shared in competence.

Concrete goal of this study is to form the debt policy profile of the EU by comparing the debt practices and development policy framework. Both of these entities include different aspects to the debt policy; debt practices include loan aid and grant aid since the 1960s, (and debt relief within grants since late 1980s) to the 2000s, development policy framework includes EU's (currently in force) statements concerning the external debt of the developing nations. These documents are the European Consensus on Development, Millennium Development Goals, Policy Coherence for Development, Intervention areas and Geographical partnerships. More itemized content is presented in chapters four and five. Overall the questions answered in this comparison concern the nature and content of the occurred changes in the debt policy. The role of the group of former colonies, African, Caribbean and Pacific ACP countries is also explored, as are the differences between donor groups; the EU and the multilateral organizations. This part also introduces the Grant–Loan

Index, which measures individually the orientation of each EU Member States' ODA as being either grant–oriented, loan–oriented, or something in between. This experimentary part of this study is a concrete example of how the data presented in this study can be applied using hypothesis–driven approach. Otherwise, the approach of this study is descriptive and "hypothesis generating" in spirit (Rosling, 2010). Although this study remains mostly in the general level as this subject has not been studied before and no previous analysis is available, more itemized and specified results are also presented.

In the debt practices part EU Member States are either (i) grouped together as one, (ii) divided into groups based on their development assistance policies, or compared as (iii) individual actors. Option (i) is used when overall development is described, and when EU is compared to other large political entities, such as the multilaterals. Option (ii) is used in most of the data analysis where differences and similarities between donors' practices are evaluated. Option (iii) is used when more detailed information is needed, concerning for example actual grant and loans sums, or the orientation of ODA.

When option (i) is used, countries included are OECD DAC member countries: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden and the UK. These are also referred to as the EU–15. Option (ii) includes three groups; the Big–3, Northern Donors and Southern Donors. Big–3 countries are France, Germany and the UK. Northern Donors are Belgium, Denmark, Finland, Ireland, Luxembourg, Netherlands and Sweden. Southern Donors are Austria, Greece, Italy, Portugal and Spain. In option (iii) countries are represented as individuals, as mentioned[1].

More specifically, the groups used in option (ii) are based on Carbone's comparison concerning the quality of EU Member States' Official Development Assistance. Carbone (2007a) divided EU Member States into four different groups based on their performance in foreign aid. The fourth group, Eastern Donors, is excluded from this study as these countries are not OECD DAC members and have not given comparable volumes of grants or loans. The division used by Carbone is (partially) based on an index developed by the Centre for Global Development, which as a measure "rewards for high volumes and letting taxpayers write off charitable contributions, but penalizes them for tying aid, for overloading recipients with too many projects and receiving debt payments from loans". (Carbone, 2007a, pg. 43) The group division by Carbone is used in this study for the concrete reason of data volume management, and the knowledge–based reason of comparing similarities between development assistance behavior and debt practice behavior. Data included in this study is vast, and managing the content of it is easier when Member States are compared in groups based on previously recognized similar attributes. Division

[1]Since the current EU has changed its formation during history on many occasions, it should be noted that all current EU–15 countries are included in data analysis since the 1960s, whether or not they have been a part of European cooperation before the European Union

to groups is also important since the volumes of given ODA differ quite substantially. Finding similarities and disparities between development assistance and debt practice behavior is one general level goal of this study. As Carbone's model measures the quality of ODA, this study measures the structure of it. The groups by Carbone are also used in the developed Grant–Loan Index, where the "fit" between Carbone's model and Grant–Loan Index is explored.

Policy Analysis

Choosing the correct research method for studying this subject requires consideration of the selected data and its type(s). Since this subject has not been studied in a comprehensive manner before, the objective of this research has to be mainly descriptive in nature.

Descriptive research often works as a prerequisite to future studies with more detailed and specific hypotheses. Descriptive study presents detailed descriptions of a certain phenomena or an event, and documents the interesting features concerning it. Descriptive study focuses on the practices, events, beliefs and processes concerning the topic and can be either qualitative or quantitative in nature, but can also include conducting surveys in the specific field. (Hirsjärvi et al., 2008, pg. 134–135).

Hodgett and Deneulin (2009) have argued that quantitative data alone is not enough to evaluate issues liked to development policy in the context of EU. They argue also that when researching policy–making, there is no distinction between qualitative and quantitative research. (Hodgett and Deneulin, 2009, pg. 66) Hirsjärvi et al concur by arguing that the relationship between qualitative and quantitative data is not competing or contradictory; use of the one does not exclude the other one. Hence, there is no clear dicotomy between the two, and the relationship between them is more like a continuum. (Hirsjärvi et al., 2008, pg. 131–133)

Therefore, this study is not specifically labeled as either qualitative or quantitative, but as coherent descriptive analysis including both aspects of the phenomena under focus; the content of the debt practices (quantitative data) and content of development policy framework (qualitative data). The selected method for this study must support vast amount of data, use of both qualitative and quantitative data, and the descriptive goal of this study. The selected method which fits the criteria is that of policy analysis.

Policy analysis is one of three fields of politics emerging in the post-behavioral period, other two are political philosophy and critical perspective to society. (Berndtson, 2008, pg. 76) The field of politics became fragmented during the 1960s when African Americans experienced subordination and the war in Vietnam was on–going, both caused widespread demonstrations in the United States. During the same time many radical young researchers combined "criticism towards society" to "criticism towards science". In the study of politics, that critique was mainly presented towards behavioralism. During this time many, for example Walker (1966) agreed that research did not respond to existing problems, but focused more on the existing and already "in place" power structures. The critical discourse following these events was named "postbehavioral revolution" by Easton in 1969. (Berndtson, 2008, pg. 76,)

Policy analysis focuses on studying political decisions and their effects. Most often its aim is to rationalize public decision–making. Most policy analysts wish to accentuate the concrete characteristics of their studies, emphasizing the link between research and "real" and acute problems. Unlike the behavioralists, policy analysts do not believe that any phenomena in politics are unchangeable or constant. Through policy analysis, the consideration of the power of government officials and organizations has gained in popularity and the stature of political institutions has emerged in pivotal role in the study of politics once again, as it was during the earliest stages of political studies. Policy analysis combined with rational choice theory is known as new political economy, and neo-institutionalism (or new institutionalism) is a separate field within policy analysis, which focuses on the relevance of public institutions to the politics of the entire society. (Berndtson, 2008, pg. 80–81)

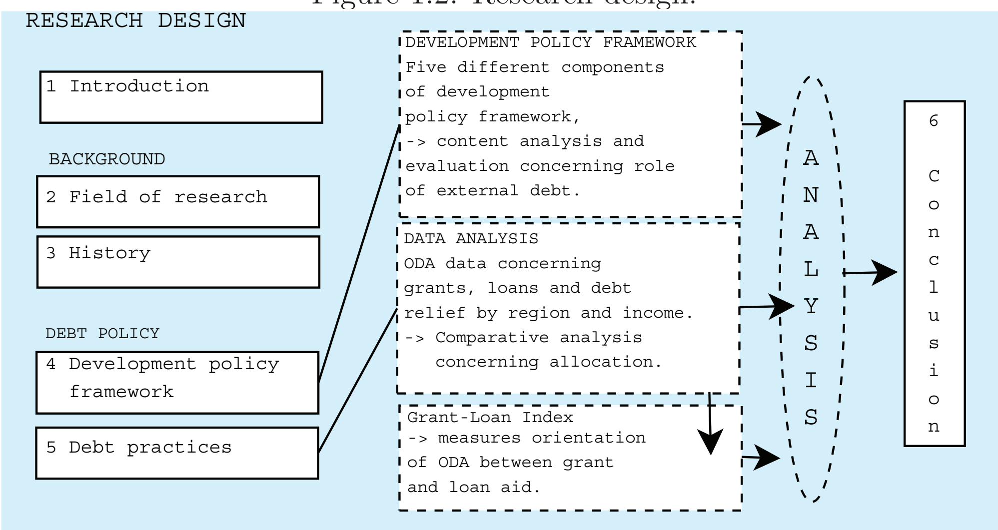
The structure of research for this Master's Thesis is derived from the policy analysts Barrien (1999) and Hill (2008). Hill (2008) has argued that *"a pattern of actions over a period of time constitutes as policy, even if these policies have not been formally sanctioned by a decision"* (Hill, 2008, pg. 8). This is the case in EU's debt policy; practices have been long on–going, but not made into an official policy.

Barrien on the other hand has provided a structure for the concrete organization of policy analysis. The traditional policy analysis includes six steps; (1) verify, define, and detail the problem, (2) establish evaluation criteria, (3) identify alternative policies, (4) evaluate alternative policies, (5) display and distinguish among alternative policies and (6) monitor the implemented policy. Traditional policy analysis also is usually either study of an existing policy, or study for policy recommendation. (Barrien 1999) In this case, the study is partially both of these, but cannot directly be labeled directly as either one. Steps of the policy analysis process are therefore revised to fit the needs of this particular study. The revised research steps are (1) verify, define and detail the problem (chapters two and three), (2) identify and analyze policy framework (chapter four), (3), identify and analyze debt practices (chapter five), (4) compare policy framework and debt practices (chapter six), (5) evaluate alternative policies (chapter six), and finally (6) evaluate overall policy (chapter six).

This Master's Thesis follows this structure of applied policy analysis and is divided in two parts; (I) background and (II) debt policy. Background part includes research step one, verifying and detailing the problem. Field of research is presented in chapter two, and history concerning the issues in chapter three. In more detail, chapters two and three of this study verify and detail the problem by discussing the dilemmas concerning loans and grants, and the overall structure of development assistance and the different factors influencing it. Although there is no particular theory tested in this study, this chapter summarizes the different theoretical perspectives pertaining to selecting different methods of development promotion. Chapter two includes EU's development policy framework structure and political economy's perspectives to aid and loans. Chapter concludes with more theoretical analysis concerning the set–up between creditors and debtors, i.e. the North and the South. Chapter three starts by explaining the most important event in history concerning the issue of external debt, the debt crisis of the 1980s. Chapter also explains the historical origins of loans, EU's delayed reaction to the debt crisis as well as proposed solutions to the problem. Chapter three concludes by analyzing the differences in policies between the Member States in the light of the historical issues presented.

Debt policy (part II) includes identifying and analyzing the policy framework and indentifying and analyzing the debt practices. EU development policy framework is presented in chapter four, and the debt practices data and its application in the form of Grant–Loan Index in presented in chapter five. Chapter four outlines the content of the EU development policy documents concerning the issue of external debt of the developing nations. Chapter five dwells into the content of these practices in detail, where statistical analysis is done in its entirety. This includes defining ODA type evolution, differences in ODA by sector, and finally analyzing the differences in loans, grants and debt relief to the developing nations by income and region. Conclusion in chapter six includes the comparison between development policy framework and the debt practices and an overall evaluation of the situation. The final chapter six includes summary of the key findings, comparison between policy content and practices, and an overview of the debt policy profile of the European Union Member States by comparing the debt practices and development policy framework content. Chapter ends with an analysis concerning the restrictions and challenges of the study. List of prolific future study areas is also given. Overall research design is presented in figure 1.2.

Figure 1.2: Research design.



More itemized data content for development policy framework is presented in

Table 1.2: EU development policy framework data content.

Debt Policy Item	Data / Source	Content	Presentation and time period	Reason for selection
Development policy framework	European Consensus on Development	Statements in Consensus concerning external debt.	Description and content analysis, signed in 2005.	Most important development policy outline document.
	Millennium Development Goals	Development goals to which the EU Member States agreed to, focus on goal 8, sub–targets 13 and 15.	Description and content analysis, signed in 2000.	MDGs include EU development policy goals.
	Other EU documents (Policy Coherence for development, intervention areas, geographical partnerships)	Other relevant documents in development policy including or excluding the issue of external debt	Description and content analysis, currently relevant documents.	Important to know in order to form a coherent perspective to issue.

table 1.2 and for debt practices data in table 1.3. Both tables include the different components of data used, what they contain, and which time period they concern, and also why they were selected for the study.

Since data is gathered in a purely technical manner from public data sources, no specific plan for specific ethical considerations is needed, as no personal or confidential data is handled. Otherwise, wider ethical perspectives are taken into consideration especially in the overall handling of data and in the process of analyzing it. The statistical data from OECD DAC has been gathered on the same day (April 11, 2010), except for ACP and non–ACP data, which was gathered later in the fall (October 10, 2010), since it was not available before that in a convenient format through the OECD DAC statistics portal.

Table 1.3: EU debt practices data content.

Debt Policy Item	Data / Source	Content	Presentation and time period	Reason for selection
Debt practices	ODA by type / OECD DAC statistics portal	Types of ODA linked to the issue of external debt	Table format including definition of types, and summary of decades when each type has appeared in the structure of ODA for the EU–15 countries, years included: 1960–2008.	ODA type data is one of two main data structures of ODA, and the development of that structure over time is highly relevant.
	ODA by sector / OECD DAC statistics portal	Sector data, focus on sector VII "Action relating to debt"	Development of the share of sector VII in overall ODA and each Member State, 1967–2008	ODA sector data is the second of two main structures of ODA, focus is on the development of sector's share in total ODA.
	Grants, loans and debt relief by region and income / OECD DAC statistics portal	Grant and loan aid given by the EU–15, debt relief included within grant aid, but also discussed as a separate item.	Presented in sums and by recipient region and income, role of ACPs and non–ACPS and differences between multilaterals and EU–15 also compared. Data from years 1960–2008.	Loans and debt relief in relation to grant aid form the core of "debt practices" data.
Grant – Loan Index	Grant – Loan Index / OECD DAC statistics portal	Index formed to measure the orientation of each EU Member States' ODA.	Comparison of EU–15 countries' grant–loan orientation as individual actors, each given points according to six variables, years 2000–2008.	Index defines each Member State current ODA practices as either grant or loan oriented, or something in between.

Part I

BACKGROUND

Chapter 2

Field of Research

The general role of a theory in a study offers a shortcut for communication. It organizes ideas and reveals assumptions, creates possibly fresh ideas, may bring about the complexity of the issue, creates explanations and predictions concerning the issue and can attest the interconnectedness of issues. (Hirsjärvi et al., 2008, pg. 135–136)

Field of research and the theoretical background for this Master's thesis includes three different entities presented in table 2.1. International Political Economy IPE field, European Union development policy field, and the North – South conflict field. Development policy field and IPE together form the core theoretical aspects, and the North – South conflict field is included to provide insight into the overall structure in which debt policy is practiced in. This chapter starts with explaining the problem of high external debt of the developing nations and over viewing the recent empirical studies concerning EU's actions in the field. After these the theoretical aspects are presented.

Table 2.1: Fields of research.

International Political Economy	EU Development Policy	North–South Conflict
Ideology and challenges of loans	Treaties and agreements	Theoretical aspects to North–South conflict
Ideology and challenges of grants	Policy evolution	International development
Political views to development assistance	Policy process	Theories of global stratification

In terms of the theoretical fields included, political economy gives the overall structure according to which action is based on. The field of international (or global) political economy summarizes differing methods of development promotion. Chapter aims to answer questions concerning the motives and reasons why a donor would choose either loans or grants as the main method of development assistance. Choosing either grants or loans or both has also been surprisingly scarcely studied (Odedokun, 2004, pg. 242–244), but general level comparison is presented. EU development policy field includes issues which explain the boundaries, outline and traditions of EU practices overall. This chapter is highly important, since EU policy field is unique in nature. I will particularly focus on questions concerning the nature of EU's development policy features and policy processes. North – South conflict field opens up the larger and wider context in which development happens through aiding and lending between countries of the North and the South. Different theories and views are overviewed, which summarize the past and present ways of conceptualizing the relationship between the developing and the developed world. As income gaps keep widening (UN Human Development Report, 2009), the perspective of the set–up between the North and the South continues to be relevant.

The different theoretical perspectives and theories included in this chapter are not tested in the customary way, since the objective of this study is not to directly examine the fit between a certain theory and actual events. The overall meaning and relationship between theory discussed in this chapter and history in the next, are summarized and explained in the context of the EU debt policy in the beginning of part II, in the beginning of chapter four, refer to figure 4.1.

2.1 Unsustainable External Debt in Development

External debt of the developing nations has been in the global agenda after the Debt Crisis of the 1980s mainly during the 1990s and the year 2000, when the massive Jubilee 2000 debt relief campaign was in process. Since then, the issue seems to have lost a lot of its appeal. What is the relevance of the issue today and is there anymore a problem with high external debt of the developing nations?

Unsustainable external debt still plays a key role in global poverty (Fikru and Getachew, 2008, Hippolyte, 2009, Befekadu, 2001) and that without debt cancellations, it is impossible to remove global poverty (Greenhill, 2009). External debt it itself External debt becomes problematic when the amount of debt exceeds country's capability of handling its loan payments. (Kraay and Nehru, 2006, pg. 341–354) Vast amount of research has been published concerning the different and more specific effects of high external debt to both social and economic development. High external debt is, however, more than just a mere economic issue, it extends to most aspects of a society. It is also an issue of democracy (Eskelinen and Sorsa, 2010, pg. 30–32), and symptom of a "skewed global financial system" (Eurodad Debt Overview, 2010).

Research concerning external debt's influence on economic development has focused on tracing the linear (or non–linear) relationship between the amount of external debt and economic growth. The prevailing understanding in this field is that whether or not the relationship between external debt and growth is linear, high amount of debt debilitates growth, and a reasonable amount of debt (in relation to income) fosters it. Studies concerning the size of debt burden have concluded that large debt burden limits growth and increase in living standards. It also lowers investments in the debtor country, and causes crowding–out phenomenon where high debt payments prevent from allocating resources to production. Crowding–out phenomena is also linked to growing uncertainty through high interest rates and inflation. (Pattillo et al., 2002, pg. 3–5)

External debt's influence on social development naturally relates to economic growth, but the social aspects of high external debt should be separately emphasized. Problems caused by high external debt in the developing nations do not also stay within the limits of the developing countries; they spread to the developed part of the world as well. George (1992) has approached this phenomenon by defining six different "boomerangs" caused by high external debt of the developing nations, which influence the societies of the Norths as well. These "boomerangs" are the environment, unemployment, drugs, immigration, taxes and conflict. These six different issues are affected by high external debt in the developing nations, but the harm caused by them spreads globally. (George, 1992) Global financial system is also affected by the debt problem. Debt situation harms commercial banks as lenders, governments as lenders and borrowers, as well as the multilateral financial institutions as lenders and borrowers, and overseers of the global economy. (Mugasha, 2007, pg. 860) In addition to generic problems caused by high debt, the system in itself has a small margin for error in loans and mistakes are common. The accumulation of large loans has been made fairly easy to the developing nations. (Wallace, 1990, pg. 229-230) Therefore, many important reasons for eradicating high and unsustainable external debt in the developing nations do exist, from the perspective of both, the developing and the developed countries.

Recent Studies

Recent studies in this specific field of debt actions of the EU Member States have not been found. Research concerning both, the reason why governments select either grants and loans and the basis for debt practices actions have been scarcely researched due to unknown reasons. Most relevant recent study found is Matthew Odedokun's (2004) comparison of multilateral and bilateral loans versus grants. Odedokun examined data from the years 1970 to 1999 for 22 donor countries and 72 recipient countries. His focus was on economic modeling of the data and the fit between mixed models of ODA. He excluded Greece, Ireland, Luxembourg, Portugal and Spain from his comparison, which are included in this study. Odedokun's focus was also global, not entirely EU–centered, and reasons for exclusion were perhaps concerned with the fact that some of these countries have not given any loans (or very little of them), such as Luxembourg and Ireland. In this study they are included as that is an important policy difference in the context of EU development policy. Odedokun's findings were focused on the different types of loans (soft loans, non–concessional loans) and grants. He concluded that grants are utilized relatively inefficiently in developing nations when compared to official loans. He also found that loans with greater concessionality (loaned with less than market value terms) are more prone to be over–borrowed. (Odedokun, 2004, pg. 256). Again, Odedokun's findings concern more the outcomes of these policies, not policy differences between EU Member States, which are under focus in in this case.

Master's Theses topics concerning the issues of external debt in the University of Helsinki have included studies concerning the effects of external debt to growth (Mäkelä, 2009), the success of HIPC and PRSP programs in the cases of Ethiopia, Senegal, Tanzania and Zambia during the years 1996–2004 (Toivio, 2006) and the Finnish concessional credit system[1] (Halonen, 2007). Mäkelä (2009) concluded that the higher the amount of external debt a country has, the least growth it will experience, i.e. high external debt hinders growth (Mäkelä, 2009, pg. 105–111). Toivio (2006) concluded that the HIPC program did not bring a sufficient solution to the debt situation in the countries examined. He concludes that despite the programs, the expenses for paying off the debt are still too high, and that the criteria defining sustainable levels of debt should be re–examined. He also states that a more coherent and effective approach should be adopted and that the current programs are not proceeding as fast as needed. Concerning the programs overall, he argues that the programs seem to be working towards keeping the countries in the peripheral position, not the opposite as promised, and that these programs are still used in the power struggle between the "North" and the "South". (Toivio, 2006, pg. 100–101) Halonen (2007) found that concessional credit emerged in the Finnish policy documents in 1996, a year after joining the EU. Most of concessional credits have been given to LMIC countries, who are able to utilize them better than poorer countries. Overall Finnish concessional credit has been able to fulfill the goals set for it. Interestingly, over half of the concessional credit from Finland during 2001–2004, and also during 1987–2006, has gone to China (Halonen, 2007, pg. 72–74). Concessional credit system is not discussed in this study as a separate item, although it is included in the country data statistics.

Recent studies concerning general EU development policy are more numerous than those concerning debt practices. These studies have been mainly oriented towards coherence, consistency and political will, see Olsen (2008), policy evolution and administrative reforms refer to Dearden (2008), aid reform see Holden (2008), enlargement's effects on the EU development policy, see Lightfoot (2008) and Vachudova (2005), and for the role of specific donors in relation to others, refer to Selberbik and Nygaard (2006) for a case of the Nordic countries, Siitonen (2005) for a case of

[1]Concessional credit in this study is an export credit for mainly Finnish made deliveries, which is supported by an interest subsidy. In this case, the interest subsidy is paid out of Finland's development cooperation budget. The recipient of the credit pays no interest. Concessional credits can be issued to Low Income Countries and Lower Middle Income Countries whose GNI (Gross National Income) per capita is less than USD 3945. However, OECD recommends that tied aid credits should not be granted to countries with the UNs Least Developed Country status and/or Highly Indebted Poor Countries (HIPC)(Finnvera, 2010)

small donors and Finland, and Carbone (2007b) for the case of Italy, for example.

Policy Coherence of Development has also been a topic increasingly discussed (Carbone, 2008), as has been the general work in EU against global inequalities (Holland, 2008), and the self–interest of EU in the development policy (Hurt, 2010). Many have also compared EU's development policy to that of other important actors. Comparison with USA, refer to Fabbrini (2008), cooperation with multilaterals, see for example Baroncelli (2009). These studies relate to this comparison in more indirect way and provide input as increasing understanding of the EU development policy field challenges.

Research concerning the role of external debt and debt sustainability in global economy has been actively and widely discussed in many contexts. Vallee and Vallee (2005) have questioned the true nature of current understanding concerning the "sustainability of debt sustainability", and call for ensuring that additional financing is made available to support long–term fiscal sustainability in low–income countries. Berr and Combarnous (2007) argue that an alternative approach to debt sustainability would be needed, since the approach adopted after the debt crisis has emphasized mainly the creditor's point of view. In more recent studies, Hernandez and Gamarra (2010) have compared debt sustainability and the currently on–going financial crisis for the IDA countries in Africa. They argue that the current debt crisis might cause a wave of defaults in the future, and that additional debt relief is needed. These studies give support and emphasize both the importance of studying EU debt policy from different perspectives, and vice versa the different perspectives of the EU donors.

What makes this study and this field especially interesting is the global financial crisis starting in 2008, which has influenced the wider context and "political environment". Although the crisis was caused by a liquidity shortfall in the United States banking system, it led to vast global consequences. This crisis is considered to be the worst financial crisis since the Great Depression of the 1930s. It has affected both the developing and the developed world and once again reminded of the importance of credit laws and policies. In Europe, Greece was the country most affected; its incautious lending practices led to a bailout by the other European Member States, see for example (Helsingin Sanomat September 19^{th}, 2010) and inspired much needed discussions concerning the development of national and also common and preventive credit policies in the EU level. Next, the theoretical aspects of the IPE are discussed.

2.2 International Political Economy and the Issue of Debt

International Political Economy IPE emerged as a subject of study in the mid–1970s. IPE has since then developed into a distinct field of International Relations. Field of International Political Economy includes many subjects, such as international finance and trade, Third World development and the North–South conflict, also environmental and gender issues have been recently included. (O'Brien and Williams, 2007, pg. 1)

Choosing the "right" or the "most appropriate" method of development promotion has been a challenge donors have faced since the beginning of development assistance. Different options range from pure grants to loans, multilateral and bilateral channels of aid, as well as debt relief and debt forgiveness. Many possible options have resulted in a situation where most often countries use not one but a mix of different development "methods", and not until recently (year 2000), has there been a shift towards favoring purely grants[2]. (Odedokun, 2004, pg. 239)

The selection of a country's own "development method" is influenced by many different political and economic issues, as well as differing development aid goals. Differing histories and financial situations between the donors have resulted in a situation where vastly differing policies are implemented by the different donors. On a separate note, in addition to the differing methods of development concerning mostly development assistance, many countries have adopted separate policies concerning their approaches towards high external debt of the developing nations. (Odedokun, 2004, pg. 239)

Eradicating the debt problem has been attempted by many different organizations and initiatives, since high external debt became "an official problem" after the initial stages of the debt crisis. These different methods have been more or less successful and they have often embodied political conditions. These programs and initiatives, such as the HIPC, Enhanced HIPC, MDRI and the Jubilee 2000 have been previously vastly studied in terms of their influence and success. See for example Claessens et al. (2007), Nwachukwu (2008), Pickup (2008), Presbitero (2009), or Shawki (2010). It is however important to recognize them as practices in which the EU Member States have participated and they are as such items included in analysis in the way they have been reported in the OECD DAC Statistics. They are also briefly discussed in chapter three, where history of external debt is discussed.

The overall tension between development assistance by grants or loans has inspired several authors. Others clearly defend grants as the primary method based on data concerning the detrimental nature of loans, while the defenders of loans argue that loans are in fact a good method, if the loan sums remain at sustainable levels. Most agree that lending to the poorest of the developing nations is pointless, as loans require a society in which the funds can be utilized well. Motives and goals

[2] This concerns global data, not just EU Member States

of giving either grants or loans also differ, and the issues concerning the method selection is discussed in more detail in the following chapter.

2.2.1 Ideology and Challenges of Loans?

The ideology behind giving loans to the developing nations stems from the liberal economic perspective to development, where loans are seen as a proper and efficient method for promoting development. Bouchet (1987) has identified five different approached to debt, within two paradigms. First approach perceives loans as mainly useful, and it includes three different perspectives. The second approach interprets loans as being mainly a negative phenomenon, and it includes two different perspectives.

Banking approach emphasizes country risk analysis, and is focused on private banks. Developing nations' credit problems are also understood as problems of the banks, since they are the mainly the creditors. Specific analysis of the economic, financial and political elements of the lending risk should be executed before lending. Bouchet states that, in reality there seems to be much lending, but not a lot of decision–making. Bouchet suggests there should be more supervision and less regulation to make this approach work in practice as well. Approach is based on neoliberal ideology. Some countries that act as bilateral creditors also emphasize country risk analysis, and lending to areas where the loans can be utilized well. (Bouchet, 1987, pg. 70,76,191)

The official approach searches for a good mix of adjustment and financing. External loans should be used to finance highly productive investments, which then, through multiplier effect, would increase income and domestic savings in the long run and that way would generate development throughout the system. Approach is based on orthodox development theory and it has been criticized to be based on an unrealistic idea of the market and biased towards the economic perspective. Approach does not take into account the links between loans, domestic economic policies and structure of development. (Bouchet, 1987, pg. 85,104–108)

The functionalist approach's focus is on the macroeconomics level, on the difference between the quantities of resources required by a developing nation versus those which are supplied to them. Economic development will happen once this gap closes and external loans are seen as a solution to make this happen. Political ideology behind this approach is value–neutral. Approach analyzes certain things superficially, such as the dynamics of power relationships between debtors and creditors. Also, the perspective has a strong normative position regarding what should be the pattern of growth in developing nations. (Bouchet, 1987, pg. 119,134,137)

Marxist approach regards debt in historical, structural and relational terms, where capital flows are seen as an instrument of dependency. External debt is interpreted to be 'the dark reverse side of development aid', which enables creditors to keep the debtors in a constant state of economic and political subjection. Approach is based on Karl Marx's Capital published in 1867. Bouchet argues that this view *"relies upon a highly deterministic model which overlooks the dimension of choice and the institution of state"*. Also, the view regards debt *"as both, the consequence and cause for exploitation"* and overlooks the fact that it is the end result of a policy choice. (Bouchet, 1987, pg. 141,152–156)

Dependency approach aims at challenging neoclassical theories, Keynesian analysis, structuralist formulations and "mechanical" Marxism and calls for a model of nondependent development. Three main points of this approach are that international finance relations are a key feature of dependency, official lending institutions are an important component of the domination structure (metropolitan centers) and the increasing participation of transnational banks in development finance lays the basis for market privatization of Third World debt. Approach's main influences have been Economic Commission for Latin America ECLA, Trotsky's Law of uneven and combined development, and also neo–Marxian analysis of the world expansion of the capitalist system. The theory itself is ambiguous regarding the conclusion of underdevelopment analysis. The approach does not give any clear solution to how the debt crisis should be solved. It also views the situation mainly from the dependency perspective, neglecting the possible opportunities loans might provide to developing nations. (Bouchet, 1987, pg. 178–179,182–184)

As is in the case of grants, motivations for giving loans are often a mix of different reasons. No current country directly represents any of the above mentioned theoretical approaches. Also, the attitudes towards loans as a form of development assistance have changed since the debt crisis (and since these approaches were outlined). It can be seen from the data analyzed in this study that there seems to be somewhat clear division between the EU Member States in terms of using loans. Some have not given any loans; some have given them for a long time. Motivations for giving loans vary highly; same outcomes can have highly differential motivations, for example not lending for moral reasons, or not lending since there are no funds to be loaned. Defining each Member State's position or loan policy is the task of this study and this definition process uses pure data in the process. Political statements and agreements have not included clear motivations or reasons for giving loans, except on a very highly level. The currently in force EU documents including such statements are discussed in chapter four.

2.2.2 Ideology and Challenges of Grants?

Using grants as the main method of development assistance has its own specific motivations, ideas and challenges. Economic aid has been one of the most prominent, persistent and enduring features of global international development activities. O'Brien and Williams (2007) identify three issues concerning aid that remain of crucial importance; motivation, effectiveness and conditionality.(O'Brien and Williams, 2007, pg. 321)

The main motivation for aid still seems to be to most self–evident reason; humanitarian. Others motives are political and economic. Giving aid is considered morally sound and right; *those that have, have to share with those who do not"* (Pearson, 1969, pg. 8). Odedokun has explored the possible theoretical frameworks suitable for the issue, and claims the selection in behalf of grants is based on mainly altruism, respect, status, and other indirect benefits relating to "gift giving". Other reasons might include the possibility of tying aid, and therefore gaining indirect but perhaps substantial benefits (Odedokun, 2004, pg. 243).

Economic reasons for giving grant aid is simply that external resources have a positive impact on local savings and growth. Aid fills the so called "savings gap" and the "foreign exchange gap" by adding resources for savings and provision of foreign exchange. Currently aid policies focus on improving economic policies, increasing the efficiency of capital and protecting the consumption of the poor. Political goals of aid may include preservation of order, peace and stability, but some might have motives closer to national interests of donors. Most often reasons for giving bilateral development assistance in the form of grants come from a combination of motivations. (O'Brien and Williams, 2007, pg. 321–322)

The idea of moral grounds for giving aid has been challenged by critics, for example by Bauer (1971) who has argued that no moral basis exists for aid giving since Western governments have primary responsibility of their own inhabitants' well–being. Critics have also argued that grants given as foreign aid go mainly to the *"pockets of the rich in the poor countries"* and that most aid is wasteful expenditure (O'Brien and Williams, 2007, pg. 321–323). Leftist critics have also brought up the dependency point of view, in which the main motivation for giving aid is perceived to be maintaining the economic and political power over the recipient countries (Hayter, 1971), and therefore being incapable of generating neither growth or development (O'Brien and Williams, 2007, pg. 323). Aid is also argued to decrease savings in the developing nations and economic motivation of donors is truly motivation for creating market shares in the recipient countries. (O'Brien and Williams, 2007, pg. 323). Koponen (1999) has also suggested not focusing on the motives behind giving grants, but more on the overall construct of what is aid as a historical and social construct (Koponen, 1999, pg. 1–2).

In addition to the actual giving of grants, much criticism has gone to the conditions attached to aid in general (including both grant as well as loan aid). Regular conditions for aid include economic conditions, such as support for exports from the donor country. Political conditions include the pursuit of foreign policy objectives and more general systemic objectives countries might have (such as promoting good governance or even neo–imperial objectives). (O'Brien and Williams, 2007, pg. 323) In addition to choosing how much grants to give and to which country, donors need to decide if and what policy conditions to set for their grants.

Debt relief as aid has been also vastly researched, mostly after the debt crisis of the 1980s. When a developing nation is unable to pay its debt, it has three options: debt forgiveness, debt restructuring, or default, i.e. they simply don't pay. In the past, European governments had an easy way of dealing with countries which used the final option of default; brute force, which led to invasion, occupation and regime changes. Nowadays, all agree that using military means to collect unpaid debt is not an option, but what should be done instead, is unfortunately not as clear. (Stiglitz, 2003, pg. 213,215). The problem is that debt relief has its own prisoner's dilemma; if a debtor country is unable to pay, banks and States are caught in a difficult situation. Each creditor is unwilling to give debt relief, for the reason that they might end up bearing the cost other debtors would not have to take part in. Each of the creditors had an incentive to be "a free rider" and let the others bear the burden of debt relief. For this reason, it is not surprising that no state or bank wanted to forgive loans of the LDCs, and the cycle of debt has kept on and will keep on going. (Balaam and Veseth, 2008, pg. 154)

However, several authors still have argued for debt relief and debt cancellation. Greenhill and Blackmore (2002), representing Jubilee Research, compared data for 10 African countries and found out that debt relief resulted in large increases in spending on education and health, and no increase in spending on defense. They found out that in 1998, spending on education was only $929 million and in 2002 it was $1306 million, more than twice the amount paid to foreign creditors. Before debt relief, more than twice as much was spend on debt service than health. Since then, spending on health has risen by 70 per cent (2002). (Greenhill and Blackmore, 2009) Greenhill and Blackmore's findings are concurred by Hassan et al. (2005) who researched the impacts of foreign loans on the economic growth of 82 severely indebted underdeveloped countries over the time period of 1991–2001. Study reveals that foreign debt has a negative and insignificant impact on the economic growth of these countries. Although debt cancellation may be less effective in the long term, based on the data, they are still supported for. (Hassan et al., 2005, pg. 61)

2.2.3 Political Views to Development Assistance

In addition to the benefits and risks of giving grants or loans to the developing nations, the selected method of aid is affected by the different political views to development aid. Different political views to aid are the realist, idealist, institutionalist and liberal perspectives. Realists interpret foreign aid to be driven by governments and used as a tool to promote national interests. Idealists see foreign aid as mainly being influenced by non–material motivations; altruism and moral obligations. Institutionalists emphasize the meaning of international organizations in the setting of the international development agenda. International organizations are useful in placing targets for the quality and quantity of aid. Liberals explore the domestic dimension of foreign aid, meaning that the pressure from domestic groups like political parties, NGOs, etc. can be more important than other reasons. (Carbone, 2007a, pg. 40–42)

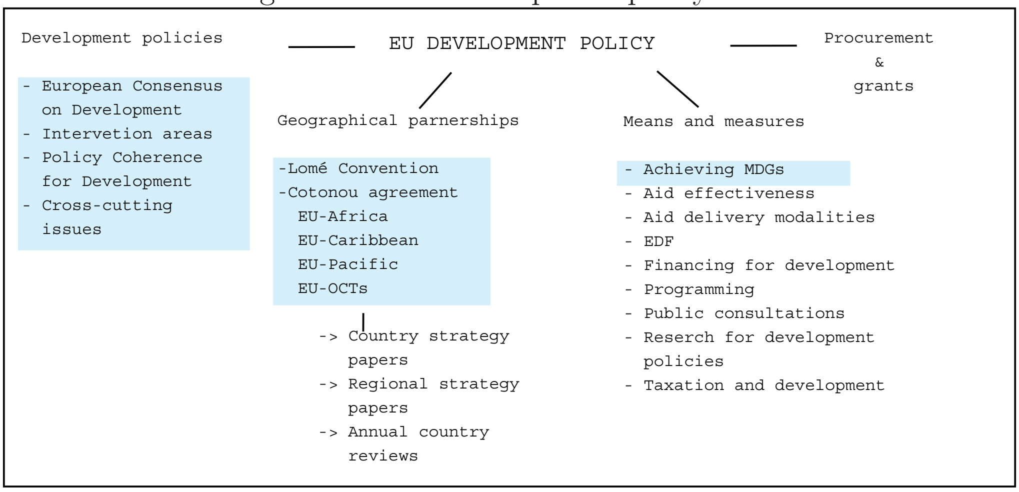
The importance of differing perspectives to development aid are emphasized when different political parties make decision concerning development practices, grants, loans or debt relief. It is important to recognize that these different aspects exist within the EU, and within all of its Member States' governments as well[3] (Hirvensalo, 2009). Next, the field of development policy in the context of the European Union is presented, especially focusing on practices and actors involved with external debt of the developing nations.

2.3 EU Development Policy and the Issue of Debt

It is important to understand the wide and complex entity of the European Union's development policy when comparing loans, grants and debt relief in development assistance and when defining and analyzing the debt practices.

Conceptualizing the EU development policy can be done is many ways, but mainly it consists of four different parts: actual development policies, geographical partnerships, means and measures of policy actualization and procurement and grants (EC Development Policy, 2009). These components and the main issues belonging under each part is listed in figure 2.1, which has those components including statements concerning debt, which are included in data analysis, highlighted in blue.

Figure 2.1: EU development policy areas.



In addition to these main parts of the development policy, the most influential documents currently guiding EU's (internal) development policy are; the European Consensus on Development, Cotonou Agreement and the EU Strategy for Africa (Kehys, 2009). Also, EU Member States have committed to the UN's Millennium Development Goals (EU MDGs, 2009) The main documents included in this study are those documents within the EU development policy which state something concerning the external debt of the developing nations. These documents are the (1)

[3]Hirvensalo (2009) representing the Ministry of Finances in Finland, concluded that for example in Finland the different political parties hold significant power over whether or not questions are brought to the agenda. For example when the Minister of Finance in Finland was from the Social Democratic party, he considered the issue to be of high importance, but later when the Minister changed to a representative of the National Coalition Party; external debt of the developing nations seems to have been removed from active discussions. (Hirvensalo, 2009)

European Consensus on Development, (2) Millennium Development Goals, (3) Policy Coherence for Development, (5) Intervention areas, and (4) Geographical partnerships. These were listed initially in chapter one, in table1.2 and they are analyzed in chapter four.

Development policy cooperation of the EU was established in the Maastricht Treaty, which was signed in 1992, and came into force in 1993. Maastricht Treaty established the legal basis for development cooperation by the EU Member States. As a result of the Maastricht Treaty, the development cooperation was clearly and fully integrated into the acquis communautaire, i.e. the legal provisions already negotiated in the earlier European treaties. Maastricht Treaty set three different objectives for development cooperation; (1) promoting social and sustainable development, (2) campaign against poverty, and (3) integration of developing countries into the world economy. (van Reisen, 2007, pg. 47). In order to further define Community responsibilities, the Maastricht Treaty and Amsterdam Treaty (1997) set out the principles of the four C's: Coherence, Complementarity, Co–ordination and Consistency. Coherence between policies that have an impact on third countries and the objectives of development cooperation, complementarity between Member States and the Commission activities in development, Co–ordination between actions of the Member States and the Commission, and Consistency between the policies of the Common European Security and Defence Policy ESDP and the development co–operation. (van Reisen, 2007, pg. 47)

In the EU there are in general three types of competences; exclusive, shared and complementary. The responsibility in the area of development cooperation is shared with the Member States.

In the case of shared competence the EU States the following:

"Member States and the Union have powers to legislate and adopt legally binding acts in a specific area. The Member States exercise their powers in so far as the Union has not exercised, or has decided to stop exercising, its competence. EU Development cooperation policy, in addition to being of shared competency, is to be reinforced by the Member States and the Union. The reduction and eradication of poverty is the primary objective of Union development cooperation policy and that this objective should be taken into account." (EU Principles, 2009)

The meaning of shared competency in the case of debt practices within the Official Development Assistance, is that EU Member governments may practice and "exercise their power" in this field freely within certain limits set by legislation. Due to this, it is expected that much variation exists in terms of debt practices between the Member States due to differences in histories, traditions and financial situation.

The content of the policy framework items are thoroughly examined in chapter four. The wider structure and evolution of the policy framework and way of actualizing development policy is discussed in this chapter by time periods. Each time period is first described overall in terms of the most relevant events, after which most important treaties and agreements are presented in detail. The most focus is given to currently in force documents and actors involved. This chapter also includes analysis concerning the nature, obstacles and challenges of policy–making in the EU, and ends with a short overview to the different actors the EU cooperated with in the field of external debt.

2.3.1 EU Development Policy Evolution

In order to fully understand the wide context involved in EU's current development policy, it is important to know the overall evolution of the EU development cooperation. The evolution and change in European development policy has been a change from colonialism to multilateralism, and a shift in focus has occurred from being Africa–centered and focused on the former colonies, to including the entire scope of developing countries (van Reisen, 2007, pg. 34,37,42) Brown identifies the three most important phases of development cooperation to be the development from EU approach to support of structural adjustment programmes in the ACP states in Lomé IV, the introduction of political conditionality into Lomé in 1990s, and the recasting of EU development cooperation in the Cotonou Agreement negotiations. (Brown, 2004)

The next chapter "History of External Debt" overviews the meaning of the historical relations between the developing nations and the EU, this chapter defines the characteristics of different time periods in development cooperation and overviews the different agreements and treaties signed since the late 1950s to the 2000s. The important role of former colonies is also discussed in both of these chapters, in this chapter the focus is on the legislative relationship between the former colonies and the EU Member States, in the following chapter the focus is on the origin of lending practices.

The former colonies have been directly and straightforwardly interlinked with the establishment of the EC and later the EU. The formation of the European Union has been a clear product of the new world order following World War II, in which the division to East and West was a key component. (van Reisen, 2007, pg. 29) The strong ties between the former colonies and European countries also are the reason why European development policy started with a strong focus on the ex–colonies. Later the focus has shifted from this group to a much wider and larger recipient group, and cooperation with multilaterals has also heavily increased. In the midst of these changes, the agreements and policies have also changed on numerous occasions.

TIME PERIOD I: 1950s to 1980s

The period between the 1950s and 1980s was limited in geographical areas as well as policy wise, but was very progressive. North–South relations were formed on the basis of two pillars: aid and trade privileges. Strong emphasis was put on the concept of partnership. (Carbone, 2007a, pg. 58) Van Reisen concludes that during this time period Europe's relations with the Third World were based upon former colonial ties. Developing world was seen as the source of energy and raw materials needed for economic development in Europe. During this time period the Treaty of Rome was signed in 1957, and it created EDF as an instrument to collectively share the burden of financial assistance to the colonies. (van Reisen, 2007, pg. 31–33). Due to the current relevance of the EDF and its link to the Cotonou Agrement, it is discussed further under "Time Period III: the 2000s". During the time period after the Second World War, a move towards cooperation with the multilaterals was made, as the International Bank for Reconstruction and Development was set up to manage the Marshall Plan. New lexicon was introduced during this time period as well; new words such as "development", "co–operation" and "partnership" were included in development policy vocabulary and development co–operation was no longer linked explicitly to the colonies. (van Reisen, 2007, pg. 29–35)

In the early 1970s was when a shift in focus started to occur. EC went from being entirely focused on associated countries, to having cooperation with non–associated areas as well. Many things had an influence on this, mainly the enlargement in 1973, when UK, Denmark and Ireland joined. This represented a turning point in EC development cooperation history; UK acted as an example of a country with highly developed relations with its (then already former) colonies. Also, the oil crisis of the 1970s added EC's interest in the countries of Middle East and Mediterranean. In 1974 Euro–Arab discussions were active, but eventually the success of those was limited since the Europeans did not want to go against the position of the United States. In 1974 the bilateral relations between some European countries and the Mediterranean were newly organized as a cohesive "Global Mediterranean Policy"). Increased activity of the Europeans in the 1970s led to new agreements and protocols on technical and financial cooperation with 17 Middle Eastern and Mediterranean countries. This cooperation included grants as well as loans. (van Reisen, 2007, pg. 38–39)

In late 1970s the scope of European development assistance widened further as Greece, Portugal and Spain joined in during the 1980s. This process extended the Latin American countries to the scope of EC's external relations. During the 1980s as the scope expanded even further, the European Parliament stated that financial and technical assistance should focus on the most poorest countries and lowest income groups in those countries. In the 1980s the importance of external aid grew exponentially in both financial and political terms; available resources increased as new countries joined, and the external cooperation was widely discussed in budget negotiations. (van Reisen, 2007, pg. 44–46)

In the early 1980s the debt crisis also emerged. It started in Latin America but spread quickly to other regions of the developing world. The overall reasons for the eruption of the crisis and Europe's reaction and proposed solutions to the events are discussed in chapter three in detail.

Many agreements were signed during this time period between the European countries and the developing nations: Yaoundé I in 1963–1969, Yaoundé II 1969–1974 (EC Yaoundé 2009), Generalized System of Preferences GSP was established in 1971 (EC GSP 2009), Lomé Conventions , trade and aid agreement in 1975/1976, Lomé I was in force during 1981–1985 and Lomé II in 1986–1990.[4] (EC Lomé, 2009)

Lomé Convention

Lomé I was for a long time the most visible and important part of the relationship between the European Community and the ACPs. Right from its "birth", it claimed to be unique. (Brown, 2004, pg. 17) The Lomé Convention set out the principles and objectives of the EEC countries and the ACP states. Lomé's main characteristics were the partnership principle, the contractual nature of the relationship, and the combination of aid, trade and political aspects. Lomé I main characteristics included non–reciprocal preferences for most exports form ACP countries to EEC; equality between partners, respect for sovereignty, mutual interests and interdependence; the right of each state to determine its own policies; security of relations based on the achievements of the cooperation system. (EC Lomé, 2009) Lomé had long–term time perspective, 5 years for Lomé I–III and 10 years for Lomé IV. Lomé I was signed in 1975, Lomé II in 1979, Lomé III in 1984 and Lomé IV in 1989. (EC Lomé 2009) Before Lomé, the Yaoundé Convention I in 1963 and II in 1969 defined the cooperation between European Economic Community and countries associated countries. First EDF was established and used in 1958–1963, when the Treaty instituting the EEC defined particular relations with the EEC Member States and the (former) colonies. (EC Yaoundé, 2009)

TIME PERIOD II: Late 1980s to Late 1990s

As the 1980s came to an end, the events in 1989 leading up to the fall of the Berlin Wall had an enormous effect on the EC in many aspects. The developments in Eastern Europe coincided with an active and sensitive phase in EC evolution and in 1992 the Maastricht Treaty established the European Union. In addition to establishing the common foreign, security and defense policy, the European Monetary Union, also development cooperation was included. (van Reisen, 2007, pg. 46) Although the formal basis of development cooperation remained and became even more poverty–focused during this time period, EU's development cooperation shifted away from the poorest countries to the Eastern European regions, as well as countries of the

[4]The reception of these agremeents and treaties in the developing nations is a highly interesting subject, but not discussed in this study due to limitations on lenght.

former Soviet Union. (van Reisen, 2007, pg. 50–51)

During this time period the ACPs had to increasingly share their aid with other regions, mostly with Eastern and Southern European areas. As the Treaty of Maastricht came into force, a stronger emphasis was put on common foreign and security policy, for which externals assistance was used as a convenient tool. During this third time period the community became more and widely involved with the developing world; its policies have overstretched and become more fragmented. This has also caused substantial criticism and problems regarding aid. (Carbone, 2007a, pg. 58)

Problems have also been caused by the debated upon position of the development cooperation in overall EU politics. The principles of coherence and consistency define the relationship between external policy areas. The principle of coherence sets out that EU policies with an impact on developing countries should be coherent with development objectives. The principle of consistency is defined as the need for the different components of EU's external policies, including development cooperation, to support overall policy objectives towards the developing world. The different components of EU's external policies are all equal and one policy field is not superior to any other. (van Reisen, 2007, pg. 49–50)

Lomé IV was in force between 1989/1990–1999 (EC Lomé 2009). The HIPC Initiative came into force in 1996, and the Enhanced HIPC in 1999. HIPC Initiatives will be later discussed in the next chapter in more detail, but in general they are joint IMF–World Bank approaches to debt reduction, which the EU Member States finance. (IMF HIPC, 2009) On a separate note, in 1990 the European Network on Debt and Development (Eurodad) of 58 NGOs working on issues related to debt, development finance and poverty reduction was established. (Eurodad intro, 2009).

TIME PERIOD III: the 2000s

The 2000s have been an interesting time period of development cooperation in terms of agreements, global cooperation and new development policy focus areas. After September 11th 2001, the Council has given higher priority to EU's security policy and some have advocated for stronger defense policy of the EU[5]. (van Reisen, 2007, pg. 50)

During the 2000s, EC development policy has become even more poverty–oriented and more efficient in the 2000s, but at the same time new kinds of security issues and trade liberalization have become fully integrated into the development field. This includes also the new ACP–EC partnership agreement, known as the Cotonou Agreement. (Carbone, 2007a, pg. 58) Cotonou Agreement came into force in 2000; it is the most comprehensive partnership agreement between developing countries and the EU. Since 2000, it has been the framework for the EU's relations with

[5] Overall development policy has been continuously under pressures of subordination to the EU's Common Foreign and Security Policy, and of being directly linked to other external issues, such as migration, security and defense. (van Reisen, 2007, pg. 60)

79 ACPs (EC Cotonou, 2009). Millennium Development Goals were also adopted in year 2000, the same year Jubilee 2000 called for massive debt relief. European Consensus on Development was signed in 2005. The multilateral Debt Relief MDRI came into force in 2006, granting 100 per cent debt relief for eligible multilateral loans from the IMF, IDA and AfDF (IMF MDRI, 2009). During the 2000s two different additional steps have been taken to reach better aid effectiveness: The Paris Declaration (2005) and the Accra Agenda for Action (2008). The Paris declaration is an international agreement to increase efforts in harmonisation, alignment, and aid management. It is a joint progress towards enhanced aid effectiveness, with five different principles: ownership, alignment, harmonization, results and mutual accountability. The Accra Agenda for Action builds on the commitments of the Paris Declaration, and includes predictability, country systems, steps concerning conditionality and untying of aid. (OECD Paris and Accra, 2010)

Cotonou Agreement

Cotonou Agreement is the most comprehensive partnership agreement between the EU and the developing countries. The Agreeements history lies in the Lomé Convention previously presented. Since 2000, it has acted as a framework for relations between the EU and 79 ACP States (former colonies). The agreement is also known as the "ACP–EC Partnership agreement". It was concluded for a twenty–year period from March 2000 to February 2020, and came into force in April 2003. Revision have been made into the agreement, first one in 2005, which came to force in July, 2008. The agreement is global in nature, and it introduces important changes and objectives to the ACP–EC cooperation. It also includes the Economic Partnership Agreements EPAs. EPAs are a plan to create a free-trade area between the EU and the ACPs(more information, refer for example to (Stocchetti, 2007). The agreement has been designed to establish comprehensive partnership between the ACP and the EC, and it is based on three complementary pillars; development cooperation, economic and trade cooperation, and the political dimension. The objective of the Cotonou agreement is to reduce and eventually eradicate poverty, these objectives are consistent with other objectives of gradual integration into the world economy and sustainable development.(EC Cotonou, 2009)

The Agreement established poverty eradication clearly the principlal objective. It also assigned a greater role for the civil society, and reinforced the political dimension of relations between the ACP countries and the EU. It also included a renegotiation for trade relations with the parties involved. (van Reisen, 2007, pg. 56)

In more detail, the Cotonou Agreement states the following concerning the goals of the partnership:

"Sustained economic growth, developing the private sector, increasing employment and improving access to productive resources shall all be part of this framework.

Support shall be given to the respect of the rights of the individual and meeting basic needs, the promotion of social development and the conditions for an equitable distribution of the fruits of growth. Regional and sub–regional integration processes which foster the integration of the ACP countries into the world economy in terms of trade and private investment shall be encouraged and supported. Building the capacity of the actors in development and improving the institutional framework necessary for social cohesion, for the functioning of a democratic society and market economy, and for the emergence of an active and organized civil society shall be integral to the approach. Systematic account shall be taken of the situation of women and gender issues in all areas – political, economic and social. The principles of sustainable management of natural resources and the environment shall be applied and integrated at every level of the partnership." (EC Cotonou, 2009)

The fundamental principles of the agreement are equality of the partnership and ownership of strategies, participation, pivotal role of dialogue and mutual obligations, and differentiation and regionalization. The actors of this cooperation include non–state actors from private sector and civil society, in addition to the states. The Cotonou Agreement is implemented mainly through the European Development Fund EDF, which is funded by the EU Member States. For the time period 2008–2013 the EDF has been allocated 22.7 billion Euros, 65% more than for the time period 2000–2007 (13.8 billion Euros). (EC Cotonou 2009). For comparison's sake, the total aid given by the EU Member States in 2008 was 70.2 billion (USD). (OECD Aid, 2010)

European Development Fund EDF

European Development Fund EDF has been in use since 1959, but due to its continuing relevance and link to the Cotonou Agreement, it is discussed here. The EDF is funded by the European Member States, and it is subject to its own financial rules. It does not come under the Community's general budget and it is managed by a committee. Each EDF has been concluded for a period of about five years, the first one started already in 1959. The 1957 Treaty of Rome made provision for the EDF's creation to grant technical and financial assistance to former colonies. Since then, it has financed the ACP and OCT states under the Yaoundé I and II, Lomé I–IV, and of course, the already mentioned Cotonou agreement and its revised version currently in force. (EC EDF, 2009)

EDF uses different kinds of financial instruments, grants, risk capital and loans to the private sector. EDF works in part in cooperation with the European Investment Bank, which will contributed a total of 1.7 billion Euros from their own resources to ACP and OCT development during the ninth EDF (2000–2007). Member States have their own bilateral agreements and do implement their own initiatives separate from the EDF and other Community funds. (EC EDF, 2009)

In addition to the agreements, actors and organizations involved with external debt are overviewed next. From within the EU structure, the European Commission (and DG Development), the ECOFIN and the European Investment Bank are discussed. From outside the EU, the World Bank, the IMF and Paris Club are briefly presented.

OTHER RELEVANT ACTORS AND ISSUES

In addition to these time periods and organizations discussed here, the actual "real life" method of carrying out development policy in the European Commission and largest multilateral organizations should to be included briefly in this discussion. Although the focus of this study is once again on the EU Member States, some important factors are to be mentioned concerning the European Commission, multilaterals and global lending market, actors with which the EU member government cooperate with.

European Commission and DG Development

"The European Commission is the EU's executive body. It represents and upholds the interests of Europe as a whole. It drafts proposals for new European laws. It manages the day–to–day business of implementing EU policies and spending EU funds. The Commission also makes sure that everyone abides by the European treaties and laws". (EC Introduction, 2010)

The European Commission is divided into several departments and services. The departments are known as Directorate–Generals (DGs). DG Development, responsible for overseeing issues concerning development policy.

EC states the following concerning DG Development:

"DG Development initiates and drafts development policy as set out in the EU Treaty. It promotes a European approach to development across the EU countries to influence international debate and work more effectively to combat poverty. The DG coordinates political relations with sub–Saharan Africa, the Caribbean and the Pacific (ACP), the African Union, regional economic communities, and the Overseas Countries and Territories in all the areas for which it is responsible, based on the Cotonou Agreement and strategies relating to those countries. In this context, DG Development drafts cooperation strategies with ACP countries and the overseas countries and territories, and coordinates and monitors funding provided through the European Development Funds and the Development Cooperation Instrument." (DG Development, 2010)

In the process of practicing its functions, DG Development works in cooperation with other Commission departments[6]. The organizational chart of the DG development has been divided on the basis of the different tasks DG Development is involved with, there are for example specific persons responsible for different parts of ACP relations, and thematic issues, such as economic development, aid programming and management, natural resources, to name a few, but no one has been specifically named to be working with issues concerning external debt. (DG Development, 2010)

In addition to DG Development, Economic and Financial Affairs Council ECOFIN is also involved with the external debt of the developing nations. ECOFIN composes of the Economics and Finance Ministers of the Member States, and also the Budget Ministers, when budgetary issues are discussed. The council meets once a month and it covers numerous EU policies including economic policy coordination, economic surveillance and monitoring Member States' budgetary policies and public finance, the Euro, financial markets, capital movements and most importantly regarding this study, the economic relations with the Third World countries. ECOFIN also prepares and adopt the budget for the EU (annually about 100 billion Euros). Decision–making in ECOFIN is by qualified majority in consultation with the European Parliament (fiscal matters are an exception, they are decided by unanimity). (Council of the EU, 2009)

European Investment Bank EIB

European Investment Bank is the EU's financing institution, its shareholders are the 27 EU Member States. EIB's board of Governors is composed of Finance ministers of the EU–27 countries. EIB provides long–term finance support in investment projects. Outside the EU, the EIB has been active in over 150 countries; it is working to implement the financial pillar of the EU external cooperation and development policies, including financial sector development, infrastructure development, security and energy supply, and sustainability. EIB is the largest international non–sovereign lender and borrower, and it works in close cooperation with EU institutions, especially the European Parliament, European Council and the European Commission. In 2009, 89% (79 billion Euros) of EIB financing went to the EU region. (EIB, 2009) The focus of this study is not on the non–governmental loans from the EU institutions, but on bilateral debt practices, and therefore the EIB is not included in analysis, but it is however identified as an interesting and important field.

World Bank and the IMF

Multilateral actors involved with the issue of developing nations' external debt are numerous. World Bank and the IMF are the most influential actors, the main difference between them is that World Bank borrows and lends, and the IMF is more of a credit union, where members have common access to a "pile of money'

[6] Mainly with DG Trade, DG External relations, EuropeAid, Humanitarian Aid Office DG ECHO and DG Enlargement

collected from the countries' individual contributions. This money can be accessed in times of need. The World Bank lends only to creditworthy governments of the developing nations. The poorer the country is, the more favorable are the terms of the loans. Nations that have a GNP per capita over $1,305 may borrow from the International Bank for Reconstruction and Development (IBRD). These loans have an interest rate slightly higher than the market rate at which the Bank itself borrows. These need to be repaid in 12–15 years[7]. Nations that have a GNP per capita under $1,305 may borrow from the IDA. Generally IDA's loans go to countries with annual per capital GNP below $865. IDA's loans are interest free and have a maturity of 35 or 40 years. (Driscoll, 2009)

Paris Club

In addition to organizations giving loans, there are separate renegotiation institutions in cases of default. In such cases, debt owed to bilaterals is renegotiated through the Paris Club. In case the same happens to multilateral debt, it is renegotiated through the Paris Club. And, finally in case debt owed to private commercial banks is not paid, it is renegotiated through the London Club. These three levels form a cohesive whole, leaving out investments in bonds and equities. (Mugasha, 2007, pg. 860)

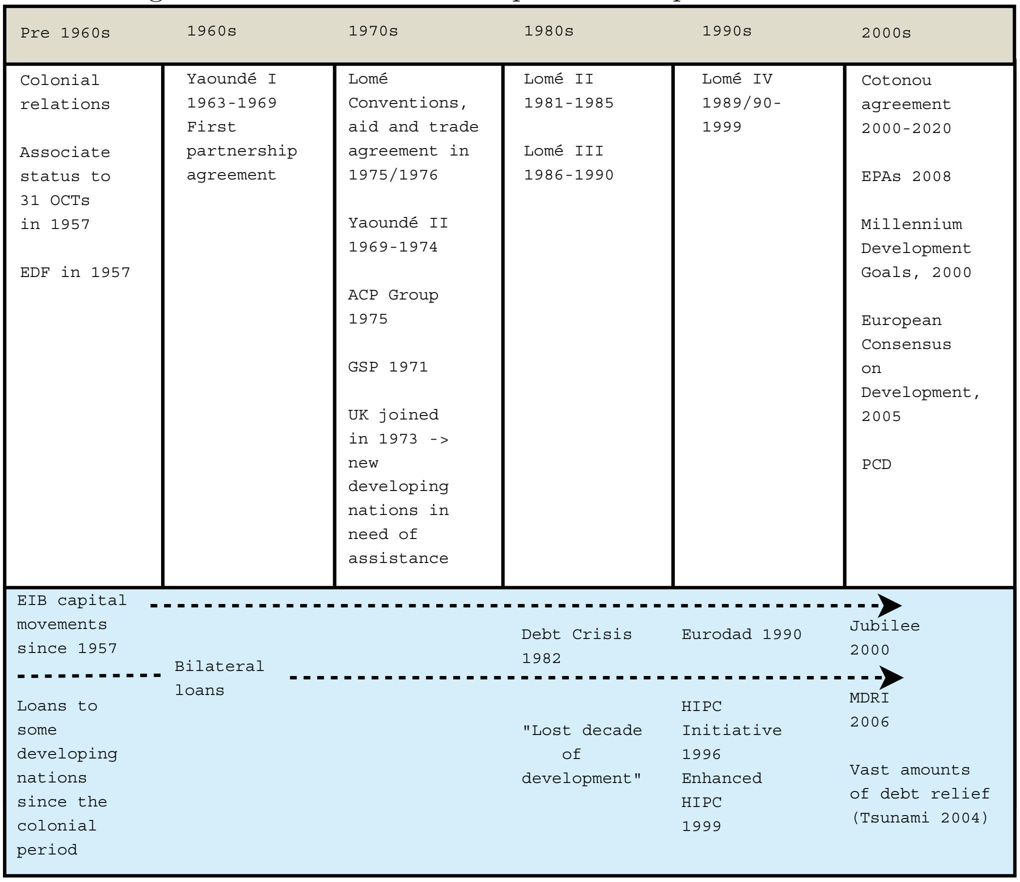
The Paris Club is an informal group of official creditors, i.e. governments. Since the year 1956, the Paris Club has reached 410 agreements with 86 different debtor countries; overall it has given 539 billion USD in loans with different terms (Paris Club, 2009). The Club's role is to find solutions to payment difficulties of the debtor countries, such as rescheduling debts or postponing the payments. The Club is very informal even though its actions are very powerful. It makes decisions on the basis of consensus and it can be described as a "non–institution". The Paris Club has no legal basis or status, and its functions are based on rules and principles agreed by the creditors. Paris Club has 19 permanent member countries. Most EU–15 countries are members, except for Greece, Luxembourg or Portugal. Paris Club offers information about loans from each creditor to each debtor and information about the terms of loans. (Paris Club 2009) London Club is the equivalent of Paris Club for commercial lenders working in the international lending market (Eurodad Debt Overview, 2010)

Figure 2.2 presents a timeline, which summarizes the most important events in both the history of development assistance and loans to the developing nations.

The different eras of development policy in the European Union's recent history as well as the evolution of the actual development policy indicate that many substan-

[7]IBRD loans in 2006 were given in total sum of $23.6 billion, the largest sector loans were allocated to was law, justice and public administration (25%), followed up with transportation (14%) and energy and mining sector (13%). Sectors with least loans were allocated to were information and communication sector (less than 1%), water, sanitation and flood protection (7%) and industry and trade (7%) (WB, 2009a, pg. 56)

Figure 2.2: Timeline of European development assistance.



tial changes have occurred over a relatively short time period. Many new agreements have been summoned and new partnerships have been proactively formed. As the history, structure and content of the development policy have been overviewed, policies in general are discussed. Next chapter overviews the process and explains how, why and what kind of policies come to exist in the EU, and explores reasons for the non–existence of a debt policy within the development policy.

2.3.2 EU Policy Process and Obstacles

The actual policy process in the EU is not comparable to any other process in global politics. It is complex nature, involves numerous actors and includes differing policy emphases of each Member State. These special features are the basis for this distinctive process, its coordination and strive for coherence. The complexity of the policy process guarantees the existence of many obstacles in policy–making, as well.

Policies in the EU can be analyzed through the different stages of the actual policy process. Member governments of the EU have access in the system in all phases: policy design, negotiation, legitimation and implementation. (Bulmer and Lequesne, 2005, pg. 29) In the traditional areas of EU policy, formal right of policy initiative and policy design rests in the Commission. However, policy proposal processes are more open and Commissions' officials have a variety of sources for proposals. Different cases in the past have shown that the success of governments' efforts in getting certain issues on the Commission's agenda depend on how far the government is willing to push the issue. Governments differ greatly in their willingness to exploit these options. In some areas of EU policy development, governments play more explicit roles in the actual framing of the policies, such as in the Common Foreign and Security Policy CFSP. (Bulmer and Lequesne, 2005, pg. 29–30) The policy negotiation process is very important regarding the use of power and influence by the Member States. The negotiation process overall includes several actors which the EU Member governments aim to influence, such as the preparatory working groups and high level groups of national officials. (Bulmer and Lequesne, 2005, pg. 30–31) Once the policy has been negotiated and agreed in the Council of the EU, they have to be legitimatized and ratified within the Member States in order for them to take effect. Policy implementation in the EU Member States has always been through agencies of one kind or another. (Bulmer and Lequesne, 2005, pg. 33–35)

In general, there are both concrete and philosophical obstacles to common policies in the EU. Main policy obstacles stem from differing policy objectives, controversial policies or past relations affecting current behavior. For example in the case of external policy, policy obstacles they can involve alliances, influence of history, etc. (Smith, 2008, pg. 10–11) The main obstacle to a common foreign policy for the EU is that the Member States insist on pursuing their foreign policy interests separately rather than as one. Member States are also interested in ensuring that the policies made in the EU cause the least damage to them as possible. It has been argued that the Member States do not share common interests and that the diversity within the systems prevents it from making agreements. There are important questions of sovereignty in this area also. The lack of cohesion weakens EU's position in the global political arena, mainly because no common military system has been created and the EU is therefore incapable of backing up its diplomacy with force. Philosophical obstacles include more generic items, such as the lack of a true "European identity", which is an effective obstacle for many common European efforts. Foreign policy for example is seen as *"the expression of the identity and interests of a particular community"*. (Smith, 2008, pg. 10–11)

In addition to policy obstacles, it is also important to evaluate why certain policies do not exist. The most prominent reason is possibly the fact that many policies, which eventually pass the system and become official, are based on the lowest common denominator (Smith, 2008, pg. 10). Forming general level policies concerning items such as loans to the developing nations faces the challenge of complementing each Member States' historical relations, preferences, and development assistance choices. Even though in the recent past actions in the field of development policy and debt practices have somewhat converged, they are still far from being consistent, as is to be shown in the data analysis. Policy coherence and coordination relating to this are discussed next.

2.3.3 EU Policy Coherence and Coordination

Since the European Union is in fact a union of 27 Member States, policy coordination is not a simple task. Each Member state has their own perspectives, views and policy agendas in each policy field. Policies in the EU are often based on the lowest common denominator, i.e. the most basic and least sophisticated level to which the members agree on. Using the lowest common denominator in policies can often weaken the Union politically. (Smith, 2008, pg. 10) In addition to policy coordination, policy coherence is also important in a union including various actors. Policy Coherence for Development (PCD) is also included in the 2005's European Consensus on Development, and included in data analysis in chapter four where development policy framework is discussed.

EU states the following concerning Policy Coherence:

"The EU shall take account of the objectives of development cooperation in all policies that it implements which are likely to affect developing countries. To make this commitment a reality, the EU will strengthen policy coherence for development procedures, instruments and mechanisms for all levels, and secure adequate resources and share best practice to further these aims." (EC Consensus, 2009, pg. 13)

Based on this statement, the non–existence of a common "debt policy" can be considered to be problematic as activity in the field does exist and has existed for a long time, and it has clearly and heavily affected the developing nations. Since development cooperation is a field of shared competence and the member governments are free to develop and choose their own practices, no such policy is expected to exist in the current EU. However, the question remains of what is the overall purpose of maintaining the shared competence in this case; to promote the free will of member governments and their own commitment to the currently in place goals of development policy? EU has itself claimed that rethinking of the way EU influences the conditions for development, is needed (EU Legislation MDGs, 2009). In 2010 it has remained evident that the goals and sub–targets of MDGs are hard to reach. In September 2010 president Obama also concluded that an altered approach to development is needed for all global actors involved (Helsingin Sanomat September 23^{rd}, 2010).

On a separate note, contradictory trends in EU policies and development cooperation are not rare. Even though the perspective of EU's development policy has been more global since the 1970s and 1980s, still in the 2000s tension exists between rival perspectives of exclusive regionalism and EU multilateralism. Exclusive regionalism supporters focuse and emphasize Africa's role in development cooperation. Multilateralism supporters on the other hand have a global focus in development cooperation, under which all developing countries fit. In the mean time still separate funds for ACP countries (in the EDF) and other developing countries exist in the EU. The Commission has proposed that the EDF would be placed under the "regular" community budget, but so far no such decision has been made. (van Reisen, 2007, pg. 56–57)

This chapter has aimed to give a concrete overview of the European development policy field. It has included both the development of the European development cooperation, and current issues relating to policies in the EU. Next, the more theoretical relationship between the North and the South is discussed.

2.4 North – South Conflict and the Issue of Debt

The relationship between the EU Member States and the developing nations can also be extended to the theoretical level, on which many different views have been presented concerning what external debt means in the interaction between the two actors. This set–up between "North" and "South" has been present in political studies, concretely and abstractly, for as long as political studies has been a separate field. Since there has been money, and unequal distribution of it, there has been also actors involved representing each side. This discussion often brings up the wide gap between the two sides, not merely concerning money, but also polices. Regulations and agreements within these policies also often appear to remain humanely distant from the concrete needs of the highly indebted and least developed countries.

Practicing international development is in fact a distinct political process where the consideration of power is essential. The liberal perspective to the issue emphasizes mutual interests between the countries in the developing and the developed nations; while the global political economists perceive that in reality there is a co–existence of common and competing interests. Issues of dominance and dependence still remain of importance and need to be discussed when discussing development promotion on a global scale. The central question in North – South relations seems to be "who speaks for whom?" Another important issue is also that who gets to frame the questions of development? Are the developing nations still passive recipients of aid, like President Truman stated in his inaugural Presidential address in 1949, or in fact active partakers in development? (O'Brien and Williams, 2007, pg. 327–328, 331)

The importance of the North–South conflict in issues concerning the question of external debt of the developing nations is especially important, since the developing nations remain in the defendant position in this discussion.

Mainly, as in the case of agreements between the EU and the developing nations, the relationships between the North and the South have been present in debates concerning finance and trade related issues. External debt has not been in focus until the 1980s.

In the 1950s demands for reform of the international trading order were common and increased aid was called for. The central platform for North–South relationships was the United Nations. North–South conflict heated in the 1970s when discussions concerning the New International Economic Order NIEO started[8]. NIEO brought a large reform, which also concerned the IMF and the World Bank[9] Developing nations criticized these international organizations for pushing the agenda of the North. Eventually many reasons influenced the failure of NIEO, but one of the main reasons was the reluctance of the North to enter into serious negotiation with the countries representing the South. During the 1980s there was discussion about how the fragmentation of the "Third World coalition" resulted in a demise of the North – South conflict, but O'Brien and Williams argue that this view fails to see the conflict set up as a structure of international political economy, which still exists. The reason for its existence is simply the income gap between rich and poor states. (O'Brien and Williams, 2007, pg. 328–329) Demeny argued in 1981, that although material progress will occur during the following decades, the demographic patterns and developments will most likely increase the income gap. (Demeny, 1981, pg. 308) Statistics presented in chapter one have shown this prediction to be accurate.

O'Brien and Williams (2007) identify debt crisis as the time period when fragmentation occurred in the "Third World coalition", which affected a new type of a relationship to be formed between the developing and the developed world. There were two different reasons for this. Firstly, the debt crisis created a range of special interests, when countries sough to battle their own debt burdens and different countries were given differential treatment in the process (some welcomed debt reduction, others were worried that it would devalue their creditworthiness). Structural adjustment programs promoting liberal economic thought severely detracted the independence of the developing nations. Secondly, the successful industrialization of some of the developing nations (NICs) is said to have exacerbated the differences among developing countries. Considering these developments and a currently more fragmented "Third World", the North – South conflict still persists and is detectable in many discussions. (O'Brien and Williams, 2007, pg. 329–331)

The problem of the North – South conflict has been conceptualized more theoretically in history by scholars representing three different theories of Global Stratification; Modernization theory (for example Rostow (1960), Dependency theory, for example Prebisch (1959), and World–Systems Theory, for example Wallerstein (1974). Whilst modernization theory examines factors internal to a country's development, dependency theory looks at relationships between countries (or groups of them), and world systems theory perceives countries always acting within a context, not as isolated entities. (Andersen and Taylor, 2006, pg. 254)

Modernization theory was developed originally in the 1960s to explain why some countries had achieved economic development, and why some had not. The theory perceives economic development as progress where traditional societies transform

[8]NIEO aimed to improve developing nations' position in global economy by changing terms of trade, increase development assistance and reduce tariffs of the developing nations, etc. (Bair, 2007) Discussions were especially active during the years 1973–1979 (O'Brien and Williams, 2007, pg. 328–329).

[9]See for example Marshall (1994), Bair (2007).

into more complex and differentiated ones (Rostow, 1960). This transformation process requires change in values, institutions as well as attitudes. Poverty is interpreted to have been a result of adherence to traditional values and customs that prevent societies from competing in a modern global economy. Modernization theory has been criticized for not being able to sufficiently take into account the relationships between countries, which do affect economic and / or social conditions[10]. (Andersen and Taylor, 2006, pg. 252)

Dependency theory understands economic development to come from the exploitation of the least powerful nations to the benefit of the wealthier countries which then control the economic and political systems of those countries. Poverty is seen to be a result of the dependence of low–income countries on wealthier nations. Prebisch (mainly influenced in the 1950s and 1960s) found that the wealth of poor nations decreased when the wealth of already developed countries increased (for more detailed information, see Prebisch 1959). Social change in societies is understood as a result of neo–colonialism and the expansion of international capitalism. (Andersen and Taylor, 2006, pg. 252)

World–systems theory, mainly developed by Wallerstein (1974), on the other hand understands economic development emerging from the development of a world market that links the core, semi–peripheral and peripheral nations. Poverty is then the result of core nations' extraction of labor and natural resources from these peripheral states. Theory's roots lie in the thinking of the dependency school and scholars such as Karl Marx and Fernand Braudel. Social change is seen to be leading to an international division of labor where increasing amount of profits is put to the hands of a few while the poorest and least powerful continue to be exploited. (Andersen and Taylor, 2006, pg. 252) Role of external debt in the up–keeping of the set–up between the core and periphery is of importance, at least according to critics of the credit system. For example George (1989) has argued that the debt crisis of the 1980s was symptomatic of *"an increasingly polarized world organized for the benefit of a minority that will stop at nothing to maintain and strengthen its control and privilege."* George argues that actors such as creditor–country governments, U.S. banks, World Bank and the IMF are working together to *"keep the Third World in line"* and that debt should be removed from financial agenda to the political agenda. (George, 1989)

Dependency theorists in general have presented arguments similar to George, by stating that the debt crisis could be perceived to be caused by the extreme dependence of the developing nations' (especially African) economies on international competitive economic conditions, over which the countries have had very little control over. The idea is that economic development of the developing nations was made impossible by the domination of world economy by the already industrialized countries. The implication is that poverty, including high indebtedness, is s result of the manner in which the countries have been integrated to the world system.

[10]See also Said (1978).

Liberal economic theory on the other hand challenges this perspective by arguing that economic liberalization as an overall process will help in increasing the flow of foreign investment into the developing countries. Loans are seen as the only way of supporting investment, but the conditions tied to them may cause even higher dependency than before. (Ikejiaku, 2008)

The theories briefly overviewed here are not about the issue of external debt, but they do give insight to where the development ideologies and opposing views have stemmed from during the time period under focus of this study. Different perspectives to economic development are present in all societies, just as are the different perspectives to loans and development cooperation as well. Most often these are also interlinked.

Relationship between the North and the South in discussions and theories seems to be especially complex due mainly to the defendant position of the developing countries and the most likely fact that majorities in North currently support neoliberal theory perspective to the debt issue. It seems that only on rare occasions the representatives of the North and the South discuss the problem together. Majorities in the developing world have experienced the problems of high debt and most likely have adopted the ideology of dependency theorists. Looking at the situation aggravated, it would seem that the it will not change until change happens in the ideological level, and when real dialogue occurs. In reality the array between the North and the South might not be as extreme as presented here, more than two different perspectives do exist. The EU Member States are a good example of countries representing the "North" with dissimilar perspectives to the matter. These differences between the Member States are explored in the data analysis of this study and in more detail in the developed Grant – Loan Index.

Chapter 3

History of External Debt

This chapter focuses on explaining the key events and time periods in history meaningful to the current and recent past relationship concerning EU Member States and the developing nations in the field of external debt. This includes mainly the origin of loans (separate stories for the existence of the idea of loans, and for metropolitans, and countries with no colonial background, giving loans to the developing nations). The point separating different perspectives of external debt can be considered to be the debt crisis of the early 1980s, which transformed the general attitude towards loans from neutral and / or positive, to mainly negative.

This chapter aims to answer questions such as how and when did the tradition of giving loans start from in general and what historical factors contribute to the currently differing policies between donors. The reasons of the debt crisis are also covered briefly, main focus is on the EU Member States' delayed reaction to the Crisis and as well as the proposed solutions. These will be later on linked to the data analysis. The chapter concludes with an analysis of the meaning of history; i.e. differing characteristics of the Member States' development assistance.

Due to limitations concerning length, main focus will be on the role of credit in the development of the global financial system and the interaction between the North and the South in their different roles as metropolitans and colonies (1400s–1900s), creditors and debtors (1400s–1980s / 2000s) and donors and recipients (1960s–2000s).

3.1 How External Debt Became a Problem?

The single most important time period in the history concerning the topic under study is the debt crisis of the 1980s. This was the time period when the first modern day developing nations' debt crisis emerged. Since then, the topic of external debt has been a heated topic on the global political agenda.

The debt crisis started in 1982 when Mexico announced it was not able to pay the substantial amounts of debt it had accumulated. This created a fear other countries would follow Mexico's lead, and soon the crisis erupted. (Balaam and Veseth, 2008, pg. 153) Debt crisis hit Sub–Saharan Africa SSA the hardest in the long run. Although several efforts were put forward to develop the continent, its share of world trade went from 1.2 per cent (1970) to only 0.4 per cent in the late 1990s. Africa's share of FDI Foreign Direct Investment also lowered; it went from 13 per cent in 1980 to less than 5 per cent in the late 1990s. Since the debt crisis began in the beginning of the 1980s, SSA's external debt went from $84.1 billion to $235.4 billion. (OECD DAC Statistics portal)

The roots of the problem were created many years before the crisis began in Mexico. The oil crises of the 1970s were one of the main influences; as the oil prices went up, so did the prices for other raw materials. The oil producing nations had plenty of extra capital to loan for different purposes. It was generally thought that technology was the solution to the developing nations' problems and that lending money for it would provide a needed solution, although eventually many of the loans turned out to be useless or used for wrong purposes. (O'Brien and Williams, 2007, pg. 222–223) The prices of agricultural products dropped around the same time oil prices peaked, and many nations were forced to lend more in order to make their original loan payments. A vicious cycle was born, and Mexico was the first one to declare it could not handle the situation. (Eichengreen and Lindert, 1992, pg. 149–153) Balaam and Veseth state that the core of the problem was *"too much had been loaned for too many"* (Balaam and Veseth, 2008, pg 153). Mugasha (2007) adds that the situation was worsened by the tightening of the monetary policy in USA, which led to high interest rates in the 1980s and occasional recessions in the economy. These reduced demand from the developing countries and deepened the crisis. Also, corrupted governments in the developing nations played a key role as did the governments in the North who were willing to lend significant sums of money. The fact that debtor governments were in some cases the main reasons for the crisis, is one key reason why some creditors overall refuse to forgive loans (Mugasha, 2007, pg. 861)

Enrique Carrasco (1999) overviewed the crisis with the following conclusions: (1) petrodollar recycling by commercial banks to developing countries gave rise to the debt crisis, (2) decreased exports and high interest rates in the early 1980s caused debtors to default on their loans, (3) debt restructuring using case–by–case method saved the international financial system from a collapse, and (4) "debt fatigue" during the mid–1980s appeared as commercial banks suggested developing nations' inability to repay might be permanent. (Carrasco, 2009)

In the Bruntland Report in 1987, the following was stated concerning loans:

"In the 1970s, Latin America's economic growth was facilitated by external borrowing. Commercial banks were happy to lend to growing countries rich in natural resources. Then major changes in international conditions made the debt unsustainable." – UN General Assembly (2009, pg. 82)

Many issues affected overall the developing nations' inability to pay the accumulated debts. Some argue that the general reason was be the failure of "developmentalist" model of the 1970s and its inability to raise productivity and hard currency export earnings. (Hoogvelt, 2001, pg. 177) Developmentalist model was effective at backing up autocratic regimes and helped in financing bureaucratic state functions. The goal was to overcome so called "international blockages", which were seen as hindrances to development. All this went beyond the financial capacity of most states and resulted in massive external debts. Unfortunately, high external debts were not the only problem, the system created bureaucratic systems, an élite and high corruption. Despite these massive problems, all this was overlooked by the international community. Hoogvelt argues this happened for two reasons; the "scientific" reason was that the global economy wanted Africa to catch up in its development, and the strategic reason was related to Cold War. Africa and other developing countries wanted to be kept on the "capitalist" side of the global political system of that time. (Hoogvelt, 2001, pg. 177) Wallerstein however opposes that the reason was the developmentalist model itself, which was easy to point to finger to. Wallerstein points out that there is always two sides to each policy; state–building can be seen as bloating bureaucracy, import–substitution industrialization can be seen as corrupt protectionism, and the before promoted state enterprises were later seen as inefficient. This new thinking eventually led to the next phase: era of globalization with the ideas of privatization and export–oriented productive activities. (Wallerstein, 2005, pg. 1265)

Overall, the debt crisis awakened governments to see that there was no central authority to oversee the system, the problems and the proposed solutions. This became officially the IMF's role, since it was already the place for last resort loans. (Mugasha, 2007, pg. 865) Its analysis of the system at that time has been claimed to be heavily influenced by multilateral banks and leading creditor governments. The main determination was, according to Simon (2002), to protect the international financial system and North's self–interest. They blamed the crisis on corruption, loss–generating state enterprises and inappropriate policies. The IMF did also take notice of the steep rise of interest rates, but did not regard it as a sufficient explanation. The banks were not held responsible for lending the so called "petrodollars". (Simon, 2002, pg. 87)

The debt crisis of the 1980s was in fact a very important phase in the history of development. Although usually the crisis is discussed in the context of the recent past, the debt problem has roots far in history, in the early traditions and histories of lending. Next chapter answers questions concerning the origin of loans and nature of early credit institutions, where the need for loans came from and how the current EU Member States differ in their histories of lending.

3.2 Histories and Traditions of Lending

European expansionist activity started in the mid 1400s and lasted until the time period after the World Wars. Origin of loans to the developing nations stem from this time period, although as such it is not considered to be the root of the current problems with high and unsustainable external debt, which are often blamed on the economic policies and practices of the 1970s and the inability to respond proactively to the causes of the debt crisis. However, this 500 year long period of colonial rule has left visible marks in history and has been especially important concerning Europe's political and economic life (Landes, 1999, pg. 422–423) and relations with the former colonies.

3.2.1 Pre–colonial Period: Origin of Loans

The starting point for loans in history is still unclear. Likely argument is that lending and borrowing have been practiced since the concept of ownership formed. Mussi (2010) Credit is sometimes considered a modern device. Although new credit forms have been developed in the "North" during the recent centuries, credit has been used already in the ancient and medieval times. Credit was "born" as an idea before industry and banking, and even before primitive forms of money. (Homer and Sylla, 2005, pg. 3) Loans can be documented at least several thousands of years back, to ancient Greek and Roman times. Monetary loans were even mentioned in the Bible. (Mussi, 2010) Loans at "interest rate" have been said to have begun when the Neolithic farmers loaned seeds and expected more back at harvest time. Old Sumerian documents dating back to 3000 B.C. reveal a systematic use of credit based loans. The recorded legal histories of several great civilizations have begun with the regulation of credit. At around 600 B.C. the legal history of Greece began with the laws of Solon. At that time big reforms to the system were needed since an economic crisis had erupted in Athens. This was partly due to excessive debt and widespread slavery for debt. The first debt cancellations and reductions were seen in Greece when also personal slavery for debt was forbidden due to the many problems they caused. (Homer and Sylla, 2005, pg. 3,17,21)

Firms granting credit to consumers and businesses have existed already in the ancient world and in the medieval Europe. (Rothbard, 2010, pg. 56) The precise origins of banking are still a subject of debate (Bordo and Cortés-Conde, 2001, pg. 45), but banking in the sense that the lent money was other people's savings, began in England in the early 17th century. (Rothbard, 2010, pg. 56) The tradition of giving loans to the developing nations from Europe stems from mainly the colonial past. Colonial past as a time period has had a substantial impact on both the current field of general development assistance as well as global economy (O'Brien and Williams, 2007, pg. 43).

During the colonial period modern monetary and fiscal policies evolved and were spread to the "New World". Colonial past is the history of capitalism and modern statehood, but also the history of long–term exploitation. This exploitation has created, through imperial pursuits, path dependence and global hegemony. Imperial–colonial ties are the believable variable in explaining the emergence of the Europeans to the global power position. (Böröcz and Sarkar, 2005, pg. 163)

Colonial time period transformed local cultures by introducing Christianity, notions of European racial superiority, and Western political ideologies, such as nationalism, liberalism and Marxism. Colonial time period's interaction between the metropolitans and the colonies was intensive, in all aspects of a society[1]. In addition to economic and political cooperation, by–products of the colonial period, such as massive slave trade, have had significant impacts on global economic and political life. (O'Brien and Williams, 2007, pg. 58–59).

The driving force behind colonizing areas has been simply to better one's condition (Duignan and Gann, 1971, pg. 23). Economic interaction between the metropolitans and the colonies had different forms and outcomes, which were eventually also political. Economic development during this time period in the colonies happened in different fields; banking systems, fiscal policies, monetary policies and of course, in the traditions of giving loans (Bordo and Cortés-Conde, 2001, pg. 1–3). Most problems in this field of economic cooperation occurred due to the clash between the "old system" of the colonies, and the "new system" of the metropolitans. Differences between local communal economies and more sophisticated colonial economies were substantial. In many cases these vast differences led to the co–existence of two separate economic or financial systems; the official and the unofficial (Ray, 1995, pg. 449). The shift from the old system to the new system required changes also in the political institutions and ways of governing (Bordo and Cortés-Conde, 2001, pg. 2–6)

Rudimentary Forms of Credit

The already "in existence" lending systems in the developing nations ranged from different forms of agricultural (rural) credit, for example in Argentina and Zanzibar, to different kinds of indigenous credit institutions, for example in West Africa. (Austin and Sugihara, 1993). Also the profession of "a moneylender"[2] existed in most of these countries (Schrader, 1994, pg. 185–187). Often credit was based not

[1]Causes for the expansion of the Europeans have been named to be greed for valued products outside Europe, fear by competition from other metropolitans (Europeans as well as Islamic forces of Egypt blocking routes to Asia), knowledge of crucial technologies enabling development of sailing ships for example, and biological "good fortune" (due to the Europeans' possession of a stock of threatening diseases and domesticated production animals). (O'Brien and Williams, 2007, pg. 58–59)

[2]During the Middle Ages, Italian moneylenders set up their benches in local marketplaces and would charge interest on their loans on a rate they themselves set. The word bench in Italian is "banca", which was where the word "bank" was derived from. If the moneylenders did not have good business in the marketplace, they would break up their benches, in Italian "banca rupta", where the word bankrupt was derived from later on. (Mussi, 2010)

on property such as land or goods, but to the security of his own person, credit was a matter of kinship (Duignan and Gann, 1971, pg. 42). Before the development of the "cash–crops" such as cocoa, credit in the modern sense was unavailable. Lending however was not unknown in the form of wealth, for example the Masai cattle–herders loaned stock. Credit of the capitalist kind was confined mainly to areas where Africans were in touch with Arabs, Europeans or Asians. Muslim peoples in Sudan were familiar with credit in different forms. (Duignan and Gann, 1971, pg. 42) Later other non–monetary forms of debt emerged in the developing nations (18^{th} and 19^{th} centuries), such as debt bondage[3], but that was already influenced by the colonial time period's slave trade. Slave trade flourished during colonial period[4] traditions (Crow and Thorpe, 1988, pg. 36–37). In some regions of Africa, where there was contact with European importers, different kinds of credit were formed, which were mainly based on the exchange and re–sale of commodities. The volume of these transactions remained however small compared to later phases when bank loans were initiated as official banking systems were established (Duignan and Gann, 1971, pg. 42) In some regions, after colonization, locals were forced to create their own informal credit markets, as the metropolitans' banks were racially discriminatory in terms of access to loans, for example in British West Africa (Austin and Uche, 2007, pg. 10) Banking institutions in Africa for example were initially confined to South Africa, where the standard Bank opened in 1862 (Duignan and Gann, 1971, pg. 42) .

3.2.2 Colonial Period: Need for Loans

In the unification process of the colonies' and metropolitans' economies was where the tradition of giving loans started for many different kinds of loans, not merely the bilateral sort. Loans, like most other things, were created out of need. Need for extra financial funds during the colonial period existed for both parties involved; the metropolitans and the colonies. Colonies' need for loans was created mainly by the metropolitans for different development endeavors[5]. Loans were used for (1) state planning and adding interest of investors, (2) helping in financing infrastructural development (mainly railroads for easing exporting and importing), (3) helping in financing wars and coping with war damages, (5) enhancing trade and productivity (6) adding purchasing power and economic opportunities in general, and (7) enhanc-

[3]Refers to a situation in which someone is forced to pay their debt by providing either services or goods to their creditor.

[4]Between the years 1450–1900 about 9–13 million slaves were transported from Africa to the Americas (O'Brien and Williams, 2007, pg. 65), but had begun before the colonial period. (Rodney, 1973, pg. 103–107)

[5]Metropolitans encouraged multiple investors, such as bankers, traders and business groups to attract investment. The British expected the colonies to pay their own way, and their government only occasionally helped in the forms of loans and grants. French and German governments put more of their own money (instead of loans) in the colonies from the beginning of the colonial period. (Duignan and Gann, 1971, pg. 8)

ing self–sufficiency. (Thompson and Adloff, 1975, pg. 128–141) Form and function of loan practices varied between metropolitans, but eventually the knowledge of differentiated practices spread widely. Interest free loans were used from early on also. It was thought that as they would promote development, the loss of the interest would be covered later by successful development. (Havinden and Meredith, 1993, pg. 140–142).

In more detail, wars did play a significant role in issues relating to debt and colonial relations, since frequent wars of the colonial period required unusual financial resources. Before wars became more frequent, financing them was easier due to the existence of "war chests", i.e. savings and the possibility to lend from either bankers or material suppliers. The idea was that paying for the debt would be easy once the war was over and the victorious party would acquire the defeated party's resources. However, when this circle was repeated several times, it led to problems as there was "nothing more to take". Many metropolitans ended up defaulting on their loans, for example Spain in the 17th and 18th centuries. (Bordo and Cortés-Conde, 2001, pg. 7–8)

Tradition of using loans to develop colonies was used by most metropolitans at some point in time; for example the British government allocated 98 per cent of its total funds going to the colonies as loans. Almost all funds before the 1920s went to railway construction, nearly all in either Central or East Africa. Most often loans did include interest payments, and they needed to be met since the beginning of the loans. After World War I, British imperialists took over colonial affairs with the aim to provide more money and possibilities on easier terms as well as comprehensive program of colonial development. Loans were given to the colonies with the idea that as they would develop, markets for British goods would also develop, enhance the purchasing power of individual inhabitants in the colonies, and produce future benefits for British trade. The overall goal of these policies was to decrease high unemployment rates in the United Kingdom. Interest free loans appeared a bit later for similar infrastructure project loans, with the justification that Britain "had to develop her possession", and also that the benefits from these projects would later surpass initial sacrifices of interest free loans. (Havinden and Meredith, 1993, pg. 140–142)

France adopted a similar approach as Great Britain. French trading companies almost entirely dominated African colonies' economies. In 1921 the colonial minister Sarraut introduced the concept of state planning, which had the goal of making France and its colonies as economically self–sufficient as they could be. Loans were a partial solution in this transformation process. French public funds were to be used to promote the colonies' productivity. The plan was abandoned at the time due to lacking finances, but revived in 1931. The depression of the time called for new economic development programs and two laws were passed in France to initiate programs of "public works" for each colony. Loans were given for the execution of these plans. They proceeded and were somewhat successful until they were interrupted by World War II. The allocated funds from France went mainly to communication, some also to the "increasing of production" and promoting the "balance of social development". Also in some areas loans were granted from funds borrowed from the local colonial administration for agricultural and transportation development needs. Coastal territories were favored over others, which led to stagnating growth inland and a mass–move towards the coastal cities. (Thompson and Adloff, 1975, pg. 128–141). Overall the French public investments in colonial Africa during the time period 1870–1936 were focused on military and port functions. Indirect loans were used in financing railroad construction, much like in Britain's case. Loans were repayable from federal revenues at interest rates ranging from 3.5 to 6.5 per cent. Overall the French African policy, including the consequences of loans, caused much critique and anti–colonialism as the policies were a growing burden on the French tax–payers. (Thompson and Adloff, 1975, pg. 133–145).

Different colonial powers had different ways of developing the credit institutions. For example, the Dutch were in a key role in spreading credit practices. Voluntary credit markets for public debt were pioneered by European cities during the Middle Ages, but the municipal practice was successfully started in the Low–countries (mainly in Holland). After its independence from Spain in the 1580s, these practices spread to the whole of Dutch Republic and were later copied by others. Monetary arrangements in Dutch colonies included for example plantation loan booms in the mid–18th century. During the same time credit facilities to planters also increased. Spanish fiscal policies were in turn much influenced by its colonial empire and France was not able to leave much of a monetary legacy for its colonies as political constraints hampered reform in its political and economic system. (Bordo and Cortés-Conde, 2001, pg. 95,135,181)

Colonial period came to an end due to different reasons and the decolonization process in itself was strenuous and had vast economic and political consequences. Some European states recognized the difficulty of continuing to rule foreign countries, in some areas the local populations waged campaigns to give up to control. Second World War was also a major factor, and the growth of nationalistic movements within the colonies had also an effect. As large number of "new" countries came into being, the balance of international organizations shifted. New organizations were established to serve the interests of the developing nations. Decolonization pushed the development issue to the international agenda, where it has ever since stayed. (O'Brien and Williams, 2007, pg. 120–121)

Bilateral lending started during the colonial period and as a method it spread widely and was used later in different development purposes. However, not all current EU–15 Member States have adopted bilateral credit practices. Next, the differences among the colonist and non–colonist EU Member States are discussed.

3.2.3 Post–Colonial Period: Emerging New Creditors

Origin of loans from the Member States with no colonial pasts is quite a different story than from former metropolitans, which had tied close relations early on with the developing nations. Traditions and ways of giving assistance in the form of loans or aid have changed, and each Member State has their own characteristics of development practices.

The eight European powers with (differing) colonial pasts[6] were Portugal, Spain, Holland (or Netherlands), Great Britain, France, Belgium, Germany and Italy. The years these countries started giving loans and which were reported in OECD statistics were; Portugal (1961), Spain (1980), Netherlands (1961), Great Britain (1961), France (1960), Belgium (1963) Germany (1960) and Italy (1961). Note here that this is not the time when the granting of loans started, but when their reporting has begun and therefore the timing of when they can be objectively studied. The remaining seven with no colonial pasts are Finland, Sweden Denmark, Luxembourg, Ireland, Austria and Greece. Luxembourg and Ireland have not given any loans for the developing nations during the entire time period under study. Greece has given some loans, but started as late as in 1998. Sweden started giving loans in 1963 and Austria a year earlier, in 1962. Finland started a decade later, in 1972. (OECD DAC, 2010)

There is more variation in the starting years for loans in the non–colonial group than the colonial group. Reasons for variation might be differences in general national development policy outlines, or in lack of finances.

Northern donor group countries' early forms of development assistance have been based on the work of church missionaries. Although many European countries acted as missionaries, the emphasis was stronger for the Northern Member States than for others. (Carbone, 2007a, pg. 46) For example, Finland has practices development cooperation for over hundred years in different forms. In the beginning it was missionary work (in Northern Namibia for example), but it wasn't until 1965 when an official office was set up for development practices. (Artto, 2009, pg. 5) This mind–set and perspective to development cooperation, and actions in the developing nations is quite far from lending and different loans practices. Other Northern donors also shared the same background, and therefore did not start lending until official development aid offices were established and different aid form and their benefits explored. In 1970 the international law on development credit came into force and an increasing number of development aid from Finland was given in the form of credit, which was also tied to purchases from Finland. In 1973 about one–third of aid was given in credit form. Later as it was noticed that the credit form aid did not function well, the policy of accentuating loans in aid was relinquished (Artto, 2009, pg. 19) and actually the law concerning development credit was overruled in Finland

[6]Differences among colonial rulers were significant, different form of direct (for example French colonies of Africa) and indirect rule (for example British colonies in Africa) were adopted. Choices of the form of rule also impacted economic relations. (Crow and Thorpe, 1988, pg. 23,27–28)

in 1992 (Finlex, 2010). Finland's case is just one example of the countries involved, others are not discussed here as there are difficulties in finding the appropriate data concerning the issue.

The differences among Member States in terms of origin of lending practices are due to the differing histories of relations with the developing nations. Countries with earlier ties in economic relations have practices also loans earlier. Countries with development aid policy background in missionary work have been introduced to lending practices later, mainly in the 1970s. This was the time period when an ideological shift in development thinking gave birth to new concrete development practices, such as international development credit and concessional credit system[7].

3.3 EU and the Debt Crisis of the 1980s

The debt crisis of the 1980s has been overviewed in the beginning of this chapter. What is especially important in this context, is how the EU Member States reacted to the debt crisis, how did it change policies and what are the differences in reactions between the Member States.

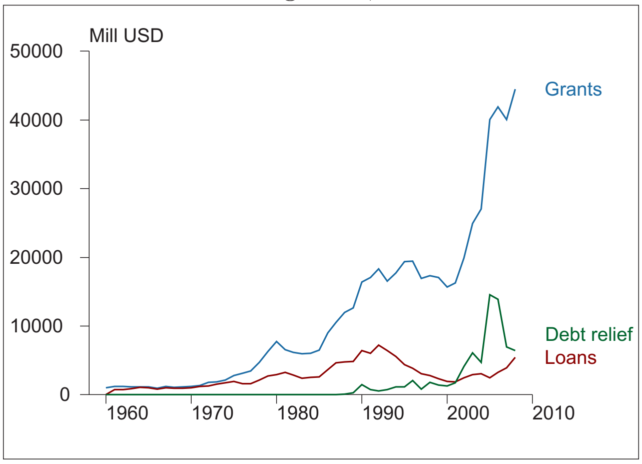
3.3.1 Reaction to the Debt Crisis

In 2010 Eurodad stated that *"A country facing debt difficulties today would run into the same problems it did three decades ago, namely meaning that there is no internationally recognized procedure to work–out sovereign debt difficulties in a fair, predictable and transparent manner."* (Eurodad Debt Overview, 2010) EU's role in the debt field was passive for a long time after the crisis erupted. In the midst of the debt crisis of the 1980's, not much happened on behalf of the Europeans. Europe did not launch any special action programs for Africa, despite the deep crisis, it did extend additional finance assistance to sub–Saharan Africa. Once it did, it did it through the international channels (IMF and World Bank), not by itself. The main reason why Europeans did not use their own channels was that they had their own on–going negotiations with African countries concerning Lomé III and did not want to get these processes confused. (Grilli, 1996, pg. 38–39)

It took several years after the eruption of the debt crisis for the EC Community to act on the issue, for some creditors it took even longer. Even though several requests and urgent need for debt reduction existed, Europeans did not react to the crisis until the year 1988, five years after the eruption of the crisis. Data concerning debt relief is discussed in chapter five, refer to figures 5.10, and tables 5.1 and 5.2. Figure 3.1 shows what the sums for loans, grants and debt releif have been and how they have developed since the 1960s. The delayed reaction to the debt crisis is well observable.

[7] For more information see for example (Halonen, 2007).

Figure 3.1: EU DAC Member States' grants, loans and debt relief since the 1960s.



In 1988, Germany, France, Italy and the UK agreed with Canada, Japan and USA to act on the crisis, and (finally) promised debt relief for African countries. The G–7 showed by taking the decision unilaterally, that the opinion of the developing nations didn't really matter. (Grilli, 1996, pg. 39) Interestingly, these four EU countries, (then EC) decided to approach other large countries, instead of the other current EC Member States. According to Grilli, this choice was made in order to share the financial burden with other major creditors instead of the "small players" of the EC. (Grilli, 1996, pg. 39)

Overall, EU's efforts, or the lack of them, need to be put in a larger global framework. One of the most important ones is EU's own political and economic interest. Mold (2007) states quite straightforwardly, that *"it is no secret that the developing countries are in a secondary place on EU's agenda"*, especially in relation to other foreign policy interests. One clear example of this is how some of the relationships with developing nations are handled at the "European level" and relations with the more important countries are handled at the national level, for example with USA or Russia. (Mold, 2007, pg. 17)

3.3.2 Solutions to the Debt Crisis

Debt crisis demanded a reaction from the global community and the European countries involved in creating the problem. That response came late after crisis, as mentioned.

Stanley Fischer presented three different kinds of options for a solution to the overall crisis in the late 1980s. First option he proposed was "muddle through", which means that simply the global community would just try to survive the situation using different methods. Second option he presented was to do a series of different agreements between each debtor and its creditors, involving both relief and lengthening of the debts. International institutions could monitor these negotiations. And thirdly, he suggested that a large international organization would be set up just for this purpose with a goal of disposing the debt problem. Mixed together, these options could have provided the needed solutions to the crisis. (Fischer, 1989, pg. 322) Fischer's ideas were only partially implemented in the actions of both the global community as well as the EU Member States for example in the Highly Indebted Poor Countries Initiative HIPC and Multilateral Debt Relief Initiative MDRI programs, explained next. Despite vast efforts of the global community, countries and non–governmental organizations, the debt problem has not been eradicated as new loans have been given and unpredictable issues have emerged. Hoogvelt argued over two dacedes later, that the debt problem still remains as the most intractable problem in the modern global economy. Since the debt crisis began in the beginning of the 1980s to the early 2000s, Sub Saharan Africa's external debt increased from USD$84.1 billion to USD$235.4 billion. (Hoogvelt, 2001, pg. 173–175)

Solutions proposed by the EU Member States in the process of solving the debt crisis can be divided in two opposing categories. Category one options offer hope to the creditors, and aims to give the expected returns from given loans, category two options aim to cancel the debts of the developing nations on the basis of need and the difficulty of the situation in the debtor countries. (Mugasha, 2007, pg. 861)

EU Member States adopted a passive role in the aftermath of the debt crisis, and as was concluded in the previous chapter, most of the solutions were developed in cooperation with the multilateral institutions. As a solution to the Crisis, the multilaterals introduced Structural Adjustment Programs SAPs and Economic Recovery Programs ERPs.

Structural Adjustment Programs SAPs

SAPs were designed to cut government expenses, reduce the extent to which the government intervenes in economy, and promote liberalization as well as international trade. SAPs did not achieve much from the point of view of national development or improving the standards of living in African countries, but they were a success when measuring the acceleration of globalization. The programs tied Africa's physical resources into servicing the "old" segment of global economy and at the same time it has transformed the financial system by which wealth is easy to transfer out of the region. Unfortunately for Africa, this removed them from the very resources they needed for dynamic adjustment to the new global economy. (Hoogvelt, 2001, pg. 184)

IMF approved SAPs were adopted and implemented in many developing nations, since they were the prerequisite for receiving financial support. The World Bank, regional development banks and most of the bilateral donors followed IMF's lead. Soon it was virtually impossible to borrow without a SAP. Extend of the control widened in 1990, when economic conditionality was accompanied by political conditionality. The aim of this was to promote "good governance" in developing nations. Based on experience, SAPs and ERPs were refined in the late 1980s and during the 1990s. Local circumstances, social aspects and negative impacts were taken into account. (Simon, 2002, pg. 88–89) During the years 1980–1989, 171 SAPs were introduced in Sub–Saharan Africa (SSA) and a further 57 by the end of 1996. Post–crisis studies have shown that SAPs have had mixed effects on poverty. (Carrasco, 2009) For example, SAPs were designed to address the debt problem, but actually led for example to the downsizing public sector, which influenced healthcare, education, etc. (O'Brien and Williams, 2007, pg. 226) The urban poor were among the worst affected. Job losses, salary cuts and high commodity price increases reduced well–being. The benefiters have been large traders, import–export merchants and agricultural producers. SAPs and ERPs have caused problems also in food security and in the environment. However, the most evident political problem has been the loss of sovereignty. (Simon, 2002, pg. 89–90)

Due to these problems, poverty reduction strategies changed when the new millennium approached. The SAPs and ERPs were replaced with Poverty Reduction Strategies PRSs. During this time development assistance was also replaced by development "cooperation". (Simon, 2002, pg. 89–90) More recent initiatives relating to debt, such as the HIPC and the MDRI are discussed next.

The HIPC and the MDRI

The HIPC and the MDRI are currently the two main global initiatives to eradicate the debt problem– Both initiatives aim to provide vast debt relief. In 2008, the committed debt relief under the HIPC was 68 billion US dollars (in nominal terms) of which 45 billion was delivered to the 23 post completion–point countries and 23 billion to the remaining interim HIPCs. The MDRI added another 43 billion in assistance to the 23 countries. Hence, the sum adds up to 112 billion USD, making their overall influence quite substantial. (Presbitero, 2009, pg. 6)

The HIPC initiative got started in 1996 by the IMF and the World Bank. Funding of the initiative is divided in half between two groups: bilateral and commercial creditors and multilaterals. Debt relief from the multilateral financial institutions is dealt with in the framework of the HIPC Trust Fund, which the World Bank manages. A variety of donators give funds for this, including the EU. (EU HIPC, 2009) In 1999, the G–7 summit decided to provide faster and more broader and comprehensible debt relief. The initiative has been extended several times, in 1998, 2000, 2002 and 2004. Since 1999, the Initiative has been known as the Enhanced HIPC. Its main aim is to reduce the debt burden of poor countries to a sustainable level. (EU HIPC, 2009) The beginning was rocky for the HIPC; the IMF set the bar high and only three countries received relief during the first four years. In the year 2000, the Jubilee 2000 movement, see for example Jubilee Debt Campaign (2009), mobilized the global community behind the issue of debt relief and a decision was made to expand the HIPC program. According to Stiglitz, after 2005, 28 countries have received more than $56 billion of debt relief, reducing the debt burden of these countries by approximately two–thirds. The HIPC did not include former Soviet Union countries and did nothing to help some of the most indebted nations, like Argentina. More relief was needed and in 2005 (at the G–8 Summit) the Members agreed to provide up to 100 per cent debt relief for the 18 poorest countries in the world, of which 14 were African. (Stiglitz, 2007, pg. 226–227)

Multilateral Debt Relief Initiative MDRI on the other hand provides 100 percent relief on debt that has been loaned from multilateral institutions to a group of low–income countries. The meaning of this initiative is to get these countries closer to the UN's Millennium Development Goals with the main focus of halving poverty by 2015. The EU supports the MDRI by financing the multilaterals and is of course, committed to the MDGs also. The MDRI goes further than the HIPC by providing full debt relief. In order to be a part of the MDRI, a country must qualify IMF terms and criteria. These include (1) macroeconomic policies; (2) implementation of a poverty reduction strategy, and (3) public expenditure management. (IMF Debt Relief, 2010)

The more recent initiatives presented in this chapter have aimed to provide an overview of the kind of actions EU Member States have taken to battle the problem caused by high external debt. These different common initiatives have been vastly studied before and are not the main focus of this study. The empirical segment of this study focuses on the bilateral actions, in which these functions fall under multilateral cooperation. This chapter is concluded next with an analysis concerning the differing development policies, which will give more insight to the meaning of history as well as participation in these endeavors.

3.3.3 National Differences between EU Member States

National differences between the Member States concerning the characteristics of external assistance are important since the differences among the EU–15 are quite substantial. Until the 1960s, France and UK were the only donors, providing assistance mainly to former colonies in Africa and Asia. During the 1960s, Germany became more active and was driven mainly by political and commercial motivations. Nordic countries got also involved but they were mainly motivated by non–material reasons. During the 1980s and 1990s, France and UK changed their policies; France normalized its relations with former colonies and Bretton Woods institutions, UK changed focus from national interests to poverty eradication. Southern Member States have become donors more recently. (Carbone, 2007a, pg. 58–59)

The differences in national histories between the EU Member States have resulted in a situation where different characteristics have been emphasized in bilateral development assistance or cooperation. The main characteristics concerning aid in general are summarized in table 3.1 for the Big–3 countries and in table 3.2 for other groups defined by Carbone (2007a). Eastern donors are included in the table, but they are not included in data analysis.

The three largest donors belonging to the Big–3 group presented in more detail are the most influential donors since their sums exceed those of other EU Member States, in some cases even multiple times. Therefore their policies are of importance.

Colonial heritage of France and UK have clearly influenced their policies, and close ties with former colonies have not vanished. All three Big–3 countries seem to have based their decisions on financial issues and the past, more so than on moral grounds, for example.

Table 3.1: Big–3: development assistance characteristics.

Term	Definition
France	Mainly driven by colonial past, closely linked to foreign policy. Relations with Africa have included aid, trade, military assistance and monetary collaboration. Supported former Soviet countries after the Cold War ended, has continued to support its former colonies. Introduced aid suspension for countries violating human rights and democracy. Lowest point in aid amounts was in 2001. Too much emphasis on education and culture, too little on the social sector. Main multilateral channel is the EC.(Carbone, 2007a, pg. 41–43)
UK	Maintained close relations with former Commonwealth nations. Has used development co–operation as a platform to support activism in international arena. Aid programme influenced by the US during the Cold War. Reductions were made in the 1980s and the 1990s. In the 1980s, was first to use conditionality for aid. Development aid became a central issue in the political agenda in the late 1990s (when labor government elected). During the new millennium it has untied aid, reallocated it to low–income countries and made Africa its priority (once again). Past years has been concerned over terrorism and international security. Main multilateral channel has been the EC. (Carbone, 2007a, pg. 43)
Germany	No strong legacy of colonialism, never favored any specific geographic area but supports middle–income countries. Significant donor since the 1960s, used aid to rebuild its image. Aid has been also driven by commercial reasons, especially to sustain heavy industries. In 1990s, amounts were reduced due to many things, such as high costs of its re–unification and increased focus on Eastern Europe. Tight fiscal situation has kept aid amounts below EU average in the 2000s, but in 2006 amounts were increased. Very high shares of total aid go to the EC. (Carbone, 2007a, pg. 45–46)

Table 3.2: Northern, Southern and Eastern donors: development assistance characteristics.

Group	Characteristics
Northern donors	Denmark, Sweden and the Netherlands are the best performers of development aid, in terms of quality and quantity. Finland is a partial exception. Northern countries have a longer tradition, which dates back to the church missionaries. Became relevant donors in the 1960s. Are not burdened by colonialism and support countries based on needs. Take active part in global development debates and cooperate with like–minded countries. They all prefer cooperation with the UN for idealistic reasons; for example, developing nations are included in the decision–making processes. The Netherlands and Finland support the efforts of the EC to coordinate development policy at the EU level, Sweden and Denmark remain more critical. (Carbone, 2007a, pg. 46)
Southern donors	Greece, Italy, Portugal and Spain do not have a long tradition of development aid. All but Italy became donors relatively late. Spain and Portugal were recipients until the 1970s and Greece until the 1980s, (explains low volumes). Aid allocation has been driven by colonial heritage. Italy started its program in the 1960s, and became a large donor in the 1980s. Since the early 1990s, has reduced aid due to internal political crisis. After 2006, has increased volume of aid a bit. Spain has emphasized commercial and cultural interests and its focus has been on Latin America. In 2004, Spain changed its focus to Africa and poverty eradication. This group donates large sums to multilaterals, aiming to increase their own influence in the arena. Group supports the EC in its efforts to coordinate development policy. (Carbone, 2007a, pg. 46–47)
Eastern donors	The Eastern group is different than the other donors. Eastern Member States which have provided aid before the collapse of the Soviet Union, are East Germany, Czechoslovakia and Bulgaria. After the collapse, all discontinued their aid and became recipients themselves. Some have managed to restart foreign aid programs, like Czech Republic and Hungary. Amounts are very small and allocation has been motivated by geographic proximity. Most concentrate on the former Soviet Union countries, the Balkans, and some communist regions. Tend to use project aid and sector–wide approaches rather than programme aid or budget support. A significant amount of aid is tied, in order to gain public and business support in return. (Carbone, 2007a, pg. 41–47)

The Southern, Northern and the Eastern donors do differ from the large donors in the Big–3 group in many ways. Northern Member States have based their actions on moral grounds more so than the large donors, starting from a early focus on the missionary work. They prefer working together with the UN and other legitimate actors and involve the developing nations more actively in decision–making. Southern Member States have emphasized other issues than the Northern states, but have suffered from financial problems which have debilitated them from giving lots of aid. Eastern Member States are new to the donor field and aim to get benefits from policy conditionality to support their own development as well.

Overall, the national differences in approaches to aid significantly matter in their approaches to debt as well. I have not found any research which would characterize EU national level differences in approaches to the debt issue, but it can be assumed that most likely that the same overall characteristics would apply to some extent. For example, countries supporting international institutions would support that they keep on taking the leading role in the debt issue. Also, countries which base their development aid decisions using moral grounds would support loan forgiveness over lending. More concrete information is needed to form a better understanding of the concrete practices and the fit between these characteristics and debt practices. Before that data is analyzed, debt in the context of development policy framework is discussed, which is followed up with the actual data analysis concerning debt practices.

Part II

DEBT POLICY

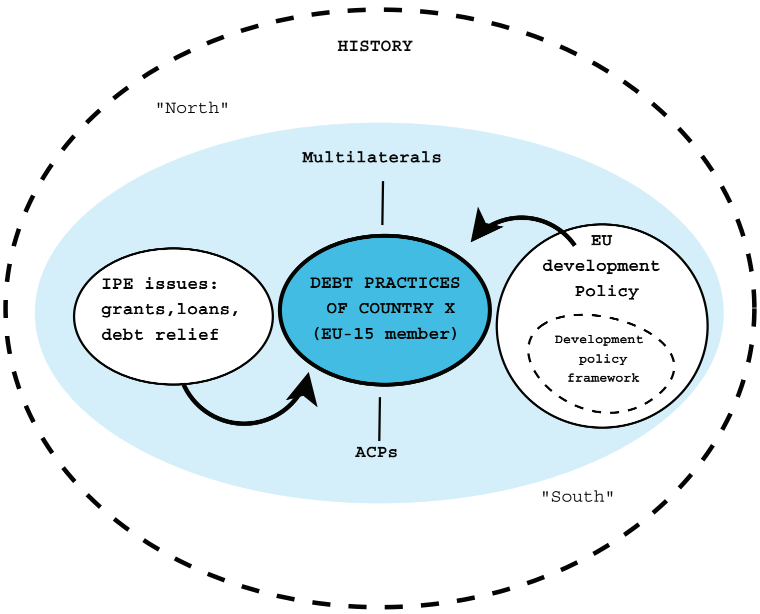
Chapter 4

Debt in EU Development Policy Framework

This chapter outlines where and how the issue of external debt of the developing nations exists in the framework of EU development policy. The framework itself includes many components, and the issue of debt is presented in them in different forms. The five components of the development policy framework discussed here are (1) European Consensus on Development, (2) UN's Millennium Development Goals, (3) Policy Coherence for Development, (4) Intervention areas, and (5) Geographical partnerships. These five areas of the development policy framework include the issues of external debt in different ways.

Part I of this study has included the theoretical perspectives influencing European debt policy, and the historical aspects relating to it. EU debt policy profile is formed in this and the following chapter, which include part II of this study.

Figure 4.1: EU's debt policy profile structure.



The content of debt policy and the relationship between the theoretical background and history is presented in figure 4.1. The specific content of the practices in the center of figure are presented in chapter five, the development policy framework content is the topic of this chapter.

What then exactly is the European Union's development policy framework? The European Union's development policy framework outlines and determines the practices possible for each country. Actual practices are also influenced by history, mainly that of the country itself, but international relations matter as well. Each EU–15 Member State has established relations with both, the multilateral organizations, and the ACPs. These relationships, between both groups, may form a highly or moderately relevant part of each Member State's debt policy and the relationship can be either active or passive. The relevancy of the relationship between the country and the ACPs in development cooperation is connected to colonial history. Activity of multilateral cooperation on the other hand is not linked to any specific events in history, but more so the traditions of each Member State. Voting powers of course differ for the EU countries, which means that the power each EU–15 Member State has in the multilateral organizations, is different[1]. (WB, 2009b) and (IMF voting power, 2009)

Since development policy is a field of shared competence, the countries may freely choose which regions and income groups they choose to finance, and how the distribution between these different groups in total ODA has and will turn out. A lot of similarities, but also some differences have occurred in this allocation over time, which will be shown in detail in chapter five. Some EU–15 countries have not given any loans to the developing nations. Some of these countries have given a lot of loans in relation to grants, and one country has even given on average more loans than grants during the time period 2000–2008. Most donors have in fact favored poorest country groups in grant allocation and, in ratio, more affluent country groups in loan allocation, and some have practiced reverse policies. Debt policy part of this study aims to describe the content of development policy framework and differences and similarities between donors and donor groups in these debt practices (chapter five). Figure 4.1 should be used in understanding the larger structure of debt policy and factors contributing to each Member States' practices. The content analysis part starts with the European Consensus on Development.

4.1 European Consensus on Development

According to the EU, the European Consensus on Development is a joint policy statement, which reflects its willingness to eradicate poverty and build a more stable

[1]EU donors have a varying amount of influence in multilateral organizations. Germany has the most voting power in the World Bank as well as in the IMF, 4.49% in IBRD, 6.49% in IDA, and 5.99% in the IMF. UK has 4.31% in the IBRD, 5.17% in the IDA and 4.94% in the IMF. France has 4.31% in the IBRD, but 4.14% in the IDA and as UK, 4.94% in the IMF. Smaller countries have much less voting power and significance overall, than the three largest donors of the Big–3 countries. (WB, 2009b) and (IMF voting power, 2009)

world (EC Consensus, 2009). The political meaning of the European Consensus on Development is enormous, because it commits the whole Union (Member States and the Community) to development policy. It provides the political orientation needed to advance the agenda of the EU. The Consensus was signed by the highest level representatives: presidents of the Council, the Commission and the Parliament in 2005. (Manservisi, 2009, pg. 7)

The adoption of the Consensus marked an important change in the role of the EU. Several Member States criticized European Commission's proposal to upgrade the 2000 EC development policy statement into an actual development strategy. Northern Member States and the UK opposed, since they wanted to maintain their right to carry out their development policies autonomously, which is an interesting point. DG Development initiated still a consultation process and presented their proposal for a statement of the EU development policy. The proposal contained two parts, one for the EC and one for the EU. Proposal for the EU also faced a lot of criticism, more than the proposal for the EC. Major difference between the proposal and the actual plan approved, was that a common thematic framework and action plan proposed DG Development did not end up in the final version. Still for the first time, the Member States had agreed on common values, principles, objectives and methods to eradicate poverty, which is a very important step in its own right. (Carbone, 2007a, pg. 55–56)

Consensus includes only three paragraphs which mention the issue of external debt of the developing nations. The statements are presented next, and a brief content analysis is given.

EU has agreed to the following statements in the Consensus on Development:

"23. Further debt relief will be considered, as well as innovative sources of finance in order to increase the resources available in a sustainable and predictable way." (EC Consensus, 2009, pg. 10)

In this paragraph the EU states that further debt relief will be considered. This implicates that as it will be under consideration, there are factors influencing that decision, what those are, is left unanswered. The mentioned innovative sources of finance are vague and need more specification. Giving more loans, or better and improved development assistance? Increasing resources might mean in fact giving more loans, or more grants, which is also left unspecified.

"28. Debt reduction also provides predictable financing. The EU is committed to finding solutions to unsustainable debt burdens, in particular the remaining multilateral debts of HIPCs, and where necessary and appropriate, for countries affected by exogenous shocks and for post–conflict countries." (EC Consensus, 2009, pg. 11)

In this paragraph the EU gives a clear statement that it is committed to seeking solutions to unsustainable debt burdens. Also, the EU states that the HIPC group is one of its main focuses regarding the debt issue. The countries that have experienced exogenous shocks and live in post–conflict stage are especially taken into account. Iraq's loans from the EU have been forgiven for the most part and also some countries that were badly damaged in the Tsunami of 2004[2]. EU particulates in this document that countries, such as the above mentioned, are supported more so than other nations in need of debt relief. Favoring countries on the basis of exogenous shocks has been criticized not to be completely fair towards countries which have been battling with debt–related problems, but have not experienced large "one–time" shocks. Favoring countries belonging to the HIPC group over those which do not, indicates that reducing loans of the countries agreeing to the political terms of the HIPC program are to be favored.

"117. Debt reduction, which is comparable to indirect budget support, with low transaction costs and a tendency to promote coordination and harmonisation between donors, could where necessary and appropriate help countries to reduce their vulnerability to external shocks." (EC Consensus, 2009, pg. 33)

This paragraph links debt reduction to the ability of a developing nation to endure external shocks. Shock resistance is highly important for all developing (and developed nations), and should be included in all development policy outlines and goals. However, shock resistance is not the only benefit of debt reduction, which should not be forgotten in this context. Reducing the amount of external debt through forgiving loans can also improve a country's ability to develop their society further, free capital for investment purposes and create more lasting solutions for sustainable development. External shocks are a risk, but many highly indebted developing nations have already other internal shocks to be prepared for, such as famine due to drought, internal conflicts, etc., which would benefit from debt reduction as well.

Overall, the Consensus includes the issue of external debt, but not in a very comprehensible manner and it is not emphasized. Next, the UN's Millennium Development goals are discussed.

4.2 UN's Millennium Development Goals

The European Union, along with most of the international community, adopted the Millennium Declaration in 2000 and agreed in it to work together in order to secure peace, security and to reduce poverty. The Millennium Declaration combines a set of interconnected and mutually reinforcing development goals into the global agenda. The main goal of the MDGs is to halve poverty by 2015. (UN MDG Report, 2009)

The Millennium Development Goals are: (1) Eradicate extreme poverty and

[2]Refer to OECD DAC (2010) for more specific country level information.

hunger, (2) Achieve universal primary education, (3) Promote gender equality and empower women, (4) Reduce child mortality, (5) Improve maternal health, (6) Combat HIV/AIDS, malaria and other diseases, (7) Ensure environmental sustainability, and (8) Develop a global partnership for development. (UN MDG Report, 2009)

Goal (8) "develop a global partnership for development" is the goal which includes the sub–targets concerning the issue of debt. The goal in itself is rather vague when compared to the other ones for example "reduce child mortality" or "achieve universal primary education". Measuring the progress in global partnership is be more challenging than measuring the reducement of child mortality, or amount of children receiving primary education. Also, the issue of external debt has been indicated to be directly linked to many of these issues, not just "global partnership" and by reducing or cancelling debts it could be less challenging to reach other goals as well.

Goal 8 and its sub–targets 13 and 15 include the following statements concerning debt:

"Target 13: *Address the special needs of the least developed countries (includes tariff–and quota–free access for exports, enhanced program of debt relief for HIPC and cancellation of official bilateral debt, and more generous ODA for countries committed to poverty reduction)*". (WB, 2009)

The actual target 13 is rather unspecific in the actual statement, but more precise in the explanation part. The mentioned special needs of the LDCs, the enhanced HIPC program and the cancellation of official bilateral debt are good and (possibly also concrete) actions needed to combat the problem. More generous ODA for countries committed to poverty reduction indicate that the countries which are willing to commit themselves to political conditions and neoliberal policies of the World Bank will be favored in ODA amounts. This is a contradictory statement considering the goal under which this sub–goal exists. Global partnership is hard to reach if and when strict political conditions are put forward. Also, the indication that countries which agree to policy changes will be favored over others is also not a way to reach global partnership, or at least it indicates that reaching global partnership will be done on the North's conditions.

"Target 15: *Deal comprehensively with the debt problems of developing countries through national and international measures in order to make debt sustainable in the long term.*" (WB, 2009)

Target 15 is overall a bit more general than target 13's explanations part, which indicated conditions for actions. This target brings forward the issue of comprehensibility and long–term sustainability, which have both been quite challenging in the past and are of course very important issues. First of all, dealing comprehensibly with something refers that an actual policy is needed and that the issue itself would be linked to all other issues it is affecting. Debt sustainability is a very important issue to be mentioned as a long term goal, but again more concrete proposals for solutions should be seeked. It is disappointing that the only concrete proposals mentioned about this issue are in target 13 and have been presented in a way which indicates policy conditioning.

According to the mid–term analysis of the UN about the MDGs, it has been stated that the share of developing countries export earnings devoted to servicing their external debt fell from 12.5 per cent (2000) to 6.6 per cent (2006). This is a good development and of course allows the countries to allocate more resources to poverty reduction. (UN Mid-Term Report, 2009, pg. 4)

EU evaluated its own progress regarding the MDGs in 2005 and concluded the following further steps: (1) set new intermediate targets for growth in official aid budgets by 2010 with a view to achieving the overall target of 0.7 per cent, (2) speed up reforms to improve the quality of aid, (3) rethink the way that the EU, through its policies, influences the conditions for development, and (4) ensure that Africa is the number one beneficiary of these new approaches and seize new opportunities for partnership between the two continents. (EU Legislation MDGs, 2009)

In 2010 it is clear that the all MDGs and their sub–targets are very hard to reach mainly due to the unexpected recession starting in late 2008. In the Millennium Summit (September 2010), USA's President Obama concluded that global actors need to alter their approach, if the Goals are to be met. If current behavior of the countries continues, Obama concluded that some improvements are made, but some of the goals will not be reached. (Helsingin Sanomat September 23rd, 2010)

The overall issue of MDGs and debt has been approached by Gunter et al. (2009) in a recent article *"towards an MDG–consistent debt sustainability concept"*. They have provided empirical evidence of a robust relationship between achieving the MDG's and having greater capacity to bear debt. Their finding is that capacity to bear debt is related to progress made in social development and also, that the capacity to bear debt shows a significant positive relationship with social development. Currently existing debt–related initiatives, like the MDRI, state that countries cannot accumulate new debt even if their debt levels are below threshold and still would remain sustainable. This has raised concerns over the fact that this framework might lead to a "low–debt, low–growth" situation. UN has proposed to *"redefine debt sustainability as the level of debt that allows the country to achieve the MDGs and reach 2015 without an increase in debt–ratios"*. UN has requested for suggestions for a conception of debt sustainability which would be more consistent with reaching the MDGs. As an overall solution, Gunter, Rahman and Shi (2009) propose debt cancellation followed by development aid. But since this might not be possible in many donor cases, it would be useful to provide more loans to countries that are able to handle more debt. (Gunter et al., 2009, pg. 269–286)

In terms of recent developments concerning the EU and the MDGs, the EU has set up a new action plan for the reaching of the MDGs. After the UN summit on the MDGs in September 2010, the EU declared that the speed for reaching the MDGs is inadequate. In 2009, total ODA in the EU was 0.42% of GNI, far from the goal set for 2010, which is 0.56%. In order to be able to reach 0.7% in 2015, as set in the MDGs, the EU has set an action plan to speed up the process of reaching the MDGs.

Action plan includes the following:

"EU countries would be called upon to produce annual action plans indicating how they will reach the 2015 targets, and to organize a yearly peer review. The member countries and the Commission should work together even more closely in developing countries to make EU aid more effective. All EU policies would be made coherent for development – trade and finance, climate change, food security, migration and security are all part of the fight against poverty. Targeted aid would focus on the goals and countries where progress is slow, particularly fragile states. The EU would develop further its partnerships with poor countries to combat climate change, rising food prices and migration, and to achieve security and financial stability."

Who would benefit and how?

Directly: hundreds of millions of people living in poverty, whose health and standard of living would be improved. Indirectly: everyone. The wellbeing of people in developing countries benefits Europeans as well."(EU Achieving the MDGs, 2010)

EU also states that the areas which have made the least progress so far have been fragile states, and areas of Sub–Saharan Africa. Current food, oil and financial crisis have scaled back development in many countries and risking the developments so far. The goals which are the most "off track" are child & maternal health, and sanitation.

These statements from the EU and the action plan itself is certainly needed in order to be able to reach the Goals set for 2015, and the added coherence called for in the actual plan altogether is a good step in the long process of developing EU development policy. In order for the action plan to succeed, a very concrete plan is needed, where roles of both donors and recipients are determined[3]. Next, other policy areas are discussed, starting from the Policy Coherence for Development.

4.3 Other Areas of Development Policy

Other documents within the development policy include Policy Coherence for Development PCD, development policy intervention areas, and geographical partnerships.

[3]For example, what is the role between the ACPs and non–ACPs in the recipient end?

The content and references to the question of debt are summarized here in order to form a coherent overall perspective to how and where the issue of external debt appears in other EU development policy documents than the widely known Consensus and the Millennium Development Goals.

Policy Coherence for Development

Policy Coherence for Development PCD gives a good example of how the issues in development policy and other fields of EU policies are conceptualized. In 2005, European Union agreed to apply the Policy Coherence for Development approach in 12 policy areas. These policy areas are thought of being able to accelerate progress towards the Millennium Development Goals. It is self–evident here that the issue of external debt or its management is not included as they are not official policies. Official Policy Coherence areas include trade, environment & climate change, security, agriculture, bilateral fisheries agreement, social policies (employment), migration, research/innovation, information technologies and transport & energy. (EU PCD, 2009)

The official idea behind PCD is to find synergies between policies other than development cooperation which have a strong impact on developing countries. The idea has stemmed from the perception that development policy formed or practiced in isolation will not bring sufficient results. The achievement of the Millennium Development Goals depends not only on aid but also on the policies defined and implemented by the EU and other international actors. Commitment towards policy coherence is also embedded in the European Consensus for Development. (EU PCD, 2009)

As mentioned, policy coherence does not include the issue of external debt or practices concerning loan allocation to the developing nations. However, as the aim of policy coherence is to find issues which have a strong impact on developing countries, practices in the field of finances could be included (trade is already on the list). The argument here is not to say that the issue should be on the list (as it is impossible since it is not an official policy), but simply to inform which items are on it. The structure and perspective to the issues influencing development could also be different.

Overall the question of policy coherence is difficult in the context of the EU considering the question of external debt. Based on the Maastricht Treaty and the formulation of PCD, the question of external debt should be included, whether or not it is a part of these 12 policy areas or not. This is based on the fact that in this context it can be understood as a question of coherence in EU's internal (development) policy. Next, the intervention areas are discussed.

Intervention Areas

The European Consensus on Development discussed earlier includes two parts; (1) EU common vision on development and (II) policy guiding the implementation of this vision at the Community level. In the Consensus it was agreed that the Community will be primarily active in nine different areas: (1) trade and regional integration, (2) environment, (3) infrastructure, communications and transport, (4) water, (5) energy, (6) rural development, territorial planning, agriculture and food security, (7) governance, democracy, human rights and support for economic and institutional reforms (8) conflict prevention and fragile states, human development, and (9) social cohesion and employment. Additional cross–cutting issues are (1) democracy, good governance and human rights, (2) gender equality,(3) environmental sustainability, and (4) fight against HIV/AIDS. (EU Debt Relief, 2010)

Area 7 includes debt relief as a part of the "support for economic and institutional reforms". Within this intervention area only the HIPC Initiative and MDRI are discussed. HIPC's aim is to reduce external debt of the poorest and most indebted developing nations to sustainable levels. So far (October 2010) 41 countries have been involved, mostly from Africa. Since June 2008, 23 countries have completed all stages of the procedure to qualify for debt relief, 10 have completed preliminary stages (decision–point) and 8 have been identified as potentially eligible [4]. The HIPC Initiative is supplemented by the MDRI, countries qualifying for the HIPC debt relief will also be granted 100% relief on eligible debt owed to all various multilateral creditors, including African Development Bank, and Inter–American Bank in addition to the World Bank and the IMF. (EU Debt Relief, 2010)

So far EU's contribution to the HIPC has been substantial when asked from the EU itself. More than 1.6 billion Euros have been pledged, of which 680 million Euros has been given as relief in its own terms and 934 million Euros has been donated to the HIPC trust fund. European Commission was the first multilateral institution to provide debt relief beyond the HIPC terms, and reserved from the European Development Fund EDF have been used for contribution to the HIPC. The HIPC program has had some encouraging results for HIPC beneficiaries, including reduction in debt and interest payments, increased spending on poverty reduction, and better management of public finances. Challenges have included the securement of full financing of the HIPC Initiative, dealing with litigation against the HIPCs by some creditors, and ensuring long–term debt sustainability. Also, dealing with exceptional cases, such as countries emerging from conflicts, has proven to be a

[4]Completion–point countries are Benin, Bolivia, Burkina Faso, Cameroon, Ethiopia, Guyana, Ghana, The Gambia, Honduras, Mali, Madagascar, Malawi, Mauritania, Mozambique, Nicaragua, Niger, Rwanda, Sao Tome & Principe, Senegal, Sierra Leone, Tanzania, Uganda and Zambia. Interim countries are Afghanistan, Burundi, Chad, Central African Republic, Republic of Congo, DR Congo, Guinea, Guinea–Bissau, Haiti, Liberia and Togo. Pre–decision–point countries are Comoros, Cõte d'Ivoire, Eritrea, Kyrgyz Republic, Nepal, Somalia and Sudan. (EU HIPC Status Report 2008, 2009)

challenge. (EU Debt Relief, 2010) On another note, the HIPC program, although highly spoken for in many EU statements, has also received criticism. For example the previously presented study by Toivio (2006) has concluded that the influence and success is controversial and inadequate in terms of being able to solve the problem of high external debt.

EU's debt relief focus has been heavily directed towards the HIPC countries. In order to be eligible for debt relief via the HIPC Initiative, policy conditions (in the form of Poverty Reduction Strategy Papers), must be fulfilled. (Presbitero, 2009) The impact and influence of the HIPC and MDRI programs have been widely discussed also in chapter two, and are not included in detail in this study. In the next chapter the geographical partnerships between the EU and some regions of the developing world are discussed.

Geographical Partnerships

The final item(s) in the development policy framework overview are the geographical partnerships. European Union has tied geographical partnerships with the ACP and OCT states (groups of former colonies and Overseas Countries and Territories). Geographical partnerships are managed through individual and regional strategy papers and progress is evaluated through annual country reviews. Separate regional strategy papers include separate programs for Africa, Caribbean and Pacific regions as well as for the OCTs. Geographical partnerships are a good concrete example in addition to the EDF, of how the former colonies and currently still associated countries have a better position in EU's development cooperation.

Africa

EU's current partnership with Africa includes the Lisbon declaration and the Joint–Africa–EU Strategy action plan (outlined in 2008). The Africa–EU strategy provides overarching long–term framework for Africa EU relations, and its first action plan has specified concrete proposals for 2008–2010. It focuses on eight partnerships; Peace and security, Democratic governance and human rights, Trade, regional integration and infrastructure, Millennium development goals (MDGs), Energy, Climate change, Migration, mobility, Employment and Science, Information Society and Space. The main objectives of EU relation with Africa is to promote the achievement of UN MDGs in the region, which will be strengthened and complemented by the specific objectives pursued within the Cotonou Agreement, for example. (EU Geographical partnerships Africa 2010)

Caribbean

EU in general has close ties with the Caribbean States, of which 16 belong to the ACP group and 15 of these have signed the Cotonou Agreement. Several EU Member States still enjoy close ties with the region, which were formed during the colonial period. In its partnership with the Caribbean, EU seeks *"growth, stability and development"*. It aims to strengthen its political partnership, support regional integration and help countries in responding to foreign competition, and help to address the region's specific vulnerabilities. These include for example natural disasters and drug trafficking. (EU Geographical partnerships Caribbean 2010)

Pacific

EU's partnership with the Pacific countries include 15 ACP countries and 3 OCTs in the Pacific region. The strategic aims of this partnership include strengthening of political dialogue, focus development cooperation on economic growth and stability and to improve the effectiveness of aid delivery. The enhanced political dialogue established between the EU and the Pacific Islands in 2008 includes security and governance, economic stability, growth and international trade, environment, development cooperation (including progress towards MDGs), and fisheries. (EU Geographical partnerships Pacific 2010)

OCTs

There are 20 overseas countries and territories linked to EU Member States (Denmark, the Netherlands, UK and France). OCT nationals are in principle EU citizens, even though the OCTs are not part of the EU or directly subject to the laws of it. The regions benefit from association arrangements, including economic and trade cooperation, sustainable development, and regional cooperation and integration. (EU Geographical partnerships OCTs 2010)

Financing for all strategic partnerships come from numerous sources, depending on the region and use. EU has aimed to use already in–existence financial instruments for the regional partnerships. European Development Fund EDF and European Investment Bank EIB are one of the main sources; finances are also derived from private sector actors as well as civil society organizations, and international organizations. Bilateral contributions from both Member States' and recipient governments are also used. Financing is provided both in the form of grants and loans. (EU geographical partnerships Africa 2010)

Overall, the geographical partnership outlines do not directly name the issue of high external debt as a focus area, but indirect references are made in two cases, those of Africa and the Pacific, which both include the reference in the form of progress towards the MDGs. The content of the more itemized country strategy papers describe cooperation more specifically, but they are not in the scope of this study due to limitations on length.

Development Policy Framework and the Issue of Debt

The peculiar thing in the framework of development policy is how the issue of external debt of the developing nations appears in the documents. Although it is of high importance in terms of actual concrete development, it is given surprisingly little emphasis. When it is discussed, it is not approached in a comprehensible manner, i.e. debt appears often in a minor role within other issues, such as within global partnership in the MDGs, not as one main problem field. It seems that it is most often either directly surpassed or only partially included in the content. The reasons for this incoherent and sporadic approach are not clear, but overall the structure of the framework could be improved in many ways when looking at the overall representation of this big problem in the policy. Literature presented earlier and the history of the issue conclude that external debt has had and will have a strong impact on development. Amount of external debt is one of the basic elements in the equation to produce development and the consequences of unsustainable debt amounts have been seen in the 1980s, and in some ways in the crisis starting in 2008 as well. Yet, the issue itself remains to be kept within the structure of development policy framework but not lifted up as one main area. Next, the actual debt practices of the EU Member States are presented and analyzed. Data included will make the role of debt practices explicit in relation to grant aid and overall development policy framework. The aim of the next chapter is to objectively compare national differences between EU–15 donors.

Chapter 5

EU–15's Debt Practices

This chapter presents the quantitative data of the debt practices in three different parts; (1) ODA evolution, (2) Loans, grants and debt relief by Region and Income, and (3) Grant – Loan Index, where national level orientation of ODA is measured. Composition of data and reasons for its selection were presented in chapter one, figure 1.3. Debt practices are defined for the EU–15 countries, since the remaining 12 Member States are not OECD DAC members and have not had debt practices. Although the focus of practices is limited to the EU–15, the importance of the lack of actions of the EU–12 is included in conclusive analysis where the overall debt policy of the EU is analyzed.

Most data has been collected from the OECD DAC statistics portal in April 2010, with the exception of the ACP data collected in October 2010 when it became available (all data which was compared was gathered on the same day to avoid any problems concerning comparability in terms of exchange rates, although the ACP data was collected later since it became available in the fall of 2010.)[1]. The groups included in data by region are Europe, Africa, America, Asia, Oceania and separate "Unspecified" group. Groups by income are the LDC (Least Developed Countries), LIC (Low–Income Countries, aka OLIC in current OECD statistics 2010, meaning other Low–Income Countries), LMIC (Low–Middle Income), UMIC (Upper Middle–Income), MADCT (ex–developing countries), and separate "Unallocated by Income" groups[2] (OECD Glossary, 2009).

Since the given grant and loans sums under focus here differ substantially between the donors, the data overview starts with presenting the actual sums of grants,

[1]Access to data on OECD DAC statistics portal, first select theme: development, select: aggregate development statistics, after which three types of statistics are available; ODA by donor, ODA by Recipient and ODA by Sector, which all have been used in this study.

[2]The sixth group included in both by region and income data comprise of funds not directly beneficial to any recipient, such as administrative costs, and research performed in donor countries for the benefit of the developing countries. Unallocated aid has risen in the past years and caused concern for the efficiency of aid in general. (Nunnenkamp et al., 2004, pg. 15) Unallocated data is included in group comparisons, although often it is simply left out of country comparisons. Here it is included since it is important to acknowledge the size of the shares going to "indirect aid" (and changes in it).

loans and debt relief from the EU–15 Member States. Data by region and income is presented in percentages by each group, but the differences in sums should be kept in mind as the policies of countries with large quantities of aid matter more.

5.1 ODA Evolution

ODA evolution chapter includes general level analysis of ODA by Type and ODA by Sector data during the time period 1960–2008 (ODA Type), and 1967–2008 (ODA Sector). Sector data is not available until the year 1967. These two data types include same data, but in different forms. Both of these data types help in understanding how the ODA structure has changed both in content and in the emphasis of the practices. ODA by Type and Sector data will describe the larger evolution of the debt practices in the context of the entire ODA structure.

ODA by Type

ODA by type data summarizes the decades when different new types of loans have been reported in OECD DAC statistics. Figure 5.1 includes summary of the new data types, the decade of their emergence and a brief description of the content of each ODA type.

Data shows that new types of loans have emerged in statistics (reporting) mainly during the 1960s and 1990s, and some in the 1970s. The 1980s and the 2000s have been slower in terms of new types of loan activities. The 1980s are also known as the lost decade of development, so the lack of new loan types is not surprising. During the 2000s old, already in existence types have been allocated more funds, such as debt relief. Figure 5.1 also lists the types of ODA as they are reported in the actual OECD DAC system. As can be seen, there are a large number of the different kinds of ODA types somehow involved with the issue of debt. This both emphasizes and concretely indicates how big of a portion of ODA is about loans or debt relief in one way or another. For the entire structure of the ODA by Type data, refer to (OECD DAC, 2010).

Since the 1960s, reported debt practices have included debt forgiveness (and debt relief grants in it), non–grant bilateral ODA, rescheduling, other lending, bilateral interest received, offsetting forgiven interest, and funds allocated to IDA, regional development banks and concessional lending. During this time lending consisted of basic practices. In the 1970s food aid loans, loans included in Associated Financing packages and multilateral interest received were added to the lists. In the 1980s no new types of loan related ODA were invented, or at least not reported in the DAC statistics. In the 1990s (mainly the year 1995) many new types emerged and some of the previous groups became main groups under which these new types were labeled under. Debt forgiveness got ODA, OOF and private claims, as well as grants for debt service reduction. Other action on debt was formed, which included service payments, debt conversions, buybacks and other debts. Loans by government, ODA

Figure 5.1: ODA types and decade of appearance in EU Development assistance.

Type of ODA loan activity	Reported in ODA Statistics since 1960s	1970s	1980s	1990s	2000s	OECD DAC Definition
I.A.1.6 Debt Forgiveness, total	x					Debt forgiveness occurs when debtor and creditor become parties to a bilateral agreement.
I.A.1.6.a. ODA Claims				x		Claims of ODA transactions by the official sector.
I.A.1.6.b. OOF Claims				x		Claims of transactions by the official sector with countries which do not meet the conditions for eligibility as ODA or Official Aid, either because they are not primarily aimed at development or because they have a grant element of less than 25%.
I.A.1.6.c. Private Claims				x		Claims of funds given by firms or private individuals.
I.A.1.6. ***Memo:Grants for debt service reduction				x		Grants for debt service reduction.
I.A.1. ***Memo:Debt Relief Grants, total	x					Total of debt relief grants.
I.A.1.7. Other Action on Debt				x		The sum of service payments to third parties, debt conversions, debt buybacks, and other.
I.A.1.7.a Service payments to third parties				x		
I.A.1.7.b Debt conversions				x		
I.A.1.7.c Debt Buybacks				x		
I.A.1.7.d Other (debt)				x		
I.A.2. Non-Grant Bilateral ODA	x					The sum of ODA lending activities, i.e. loans by government or official agencies.
I.A.2.1. Loans by government				x		Sum of food aid loans, rescheduling loans, and other lending.
I.A.2.1.a. Food aid loans		x				Loans for food aid.
I.A.2.1.b. Rescheduling,total	x					The sum of rescheduled ODA claims and OOF claims.
I.A.2.1.b.i. ODA Claims (capitalized interest)				x		Claims of ODA.
I.A.2.1.b.ii. OOF Claims				x		Claims of OOF.
I.A.2.1.c. Other lending	x					All ODA loans to other than food aid or rescheduling loans.
I.A.2.1.4. Offsetting debt reorganization				x		Offsetting entries to avoid double counting.
I.A.2 ***Memo:Loans inclu. in A.F.Packages		x				Loans included in Associated Financing packages.
I.A.2.***Memo:Interest received bilateral	x			x		The total of actual bilateral interest receipts from developing countries, including interest.
I.A.2.***Memo:Offsetting forgiven interest						Interest forgiven ODA loans.
I.B.1.3. To IDA	x					Funds allocated to IDA.
I.B.1.5. To Regional Development Banks	x					Grants and capital subscription to regional development banks.
I.B.2. Concessional lending	x					Loans at ODA terms.
I.B.***Memo:multilateral interest received		x				Interest received by the reporting country on its concessional loans to multilateral institutions.
I. ***Memo:(bil+mul):HIPC Initiative				x		Total amount of contribution to the HIPC Initiative.
I. ***Memo:(bil+mul):IDA Debt Reduction Facility					x	Total amount of contribution to the IDA Debt Reduction Facility.

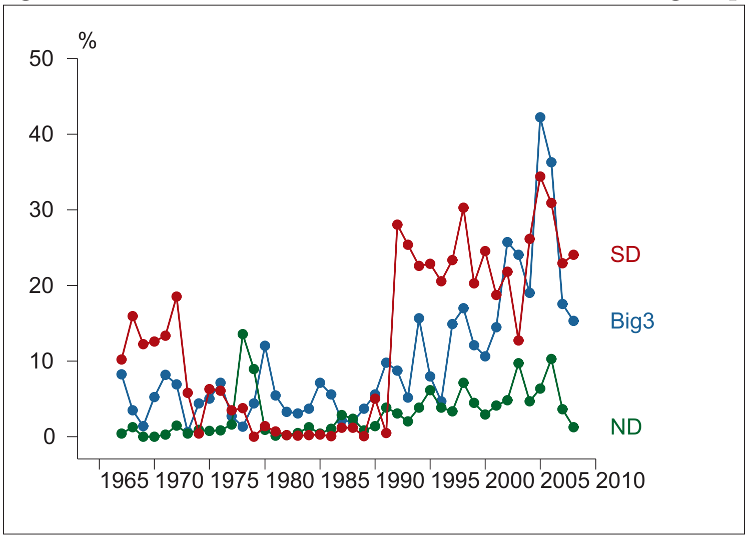
claims, OOF claims, offsetting debt organization were labeled under non–grant bilateral ODA. And finally, the HIPC was included in statistics. In the 2000s the only addition has been a memo of IDA Debt Reduction Facility funds.

Overall a move from ”basic practices” of the 1960s and 1970s to more complex system of the 1990s is easily observable according to this data due to the increasing amount of practices labeled under previously existing data types. The enthusiasm to develop the loan system more in the 1990s is most likely linked to the establishment of the EU in 1995 (when most of the new types emerged, also the year when EU was established). Other possible reason is the enlargement during the same year. Due to restrictions on length, the differences between EU Member States in terms of new loan types in ODA is not examined here in depth, but it is recognized as an important and interesting field to be explored. Next, ODA by sector data is presented, where more detailed information is given concerning the share of loan related practices in ODA of the EU Member States, by donor groups and by individual donor countries.

ODA by Sector

ODA by sector data includes 12 different sectors of ODA. Sectors are: I. Social Infrastructure & Services, II. Economic infrastructure and Services, III. Production Sectors, IV. Multisector / Cross–Cutting, V. Total sector allocable (I+II+III+IV), VI. Commodity aid and general program assistance, VII. Action Relating to Debt, VIII. Humanitarian Aid, IX. Administrative costs of donors. X. Support to NGO’s, XI. Refugees in Donor Countries and XII. Unallocated/Unspecified (OECD DAC, 2010).

Figure 5.2: Sector VII means for the three donor groups.

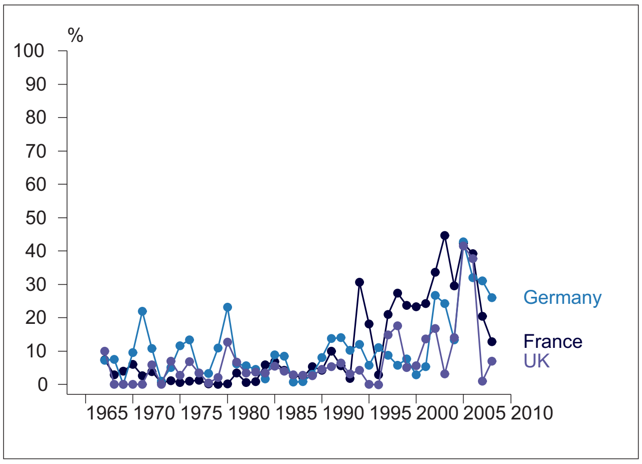


The focus here is on sector VII’s ”Action relating to Debt” development for the three donor groups in percentage shares. This sector includes all actions relating to debt: debt forgiveness, debt conversions, swaps, buy–backs, rescheduling and refinancing.

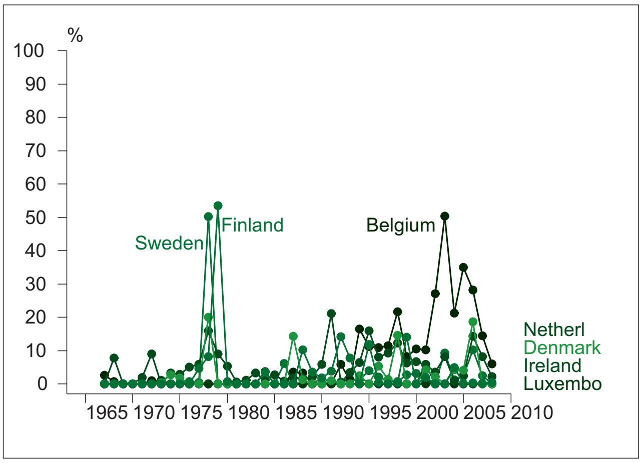
Sector VII mean shares in ODA are presented in figure 5.2, individual country shares for each donor group are presented in figure 5.3. As can be seen from data concerning sector VII’s mean shares in ODA for the three donor groups, there are differences between the donor groups.

Since means can often hide relevant information, the actual shares of sector VII in ODA of each EU–15 country are presented. From this general comparison it can be seen that SDs have had higher shares during the late 1960s as well as early 1990s. Share of sector has been surprisingly low during the 1980s. Northern donors have had the lowest shares on average during this time period (except in 1978).

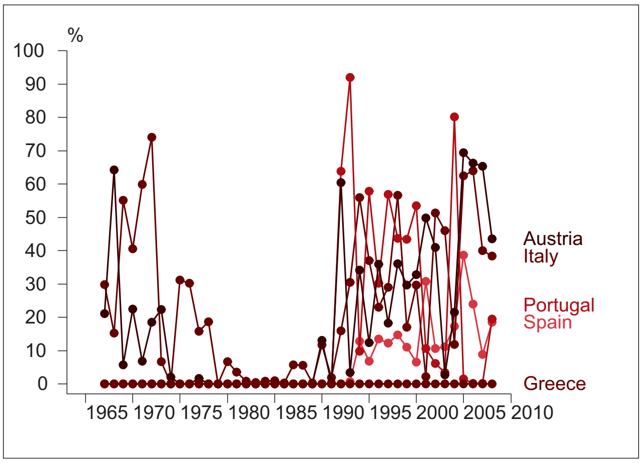
Figure 5.3: Sector VII shares in ODA for the three donor groups (1967–2008).



(a) Big–3



(b) Northern donors



(c) Southern donors

Figure 5.3 shows well what kind of variation is hidden behind mean calculations. Southern donors have in reality much higher percentages of sector VII in ODA (Greece has not given any loans, which affected mean data results). What is also interesting here between the groups is the high variation of the shares of the SD group in both actual percentages and between time periods. Big–3 group on the other hand has had much less variation between the donors. Still it should be noted that the shares of Sector VII have grown for the Big–3 group during the 1990s and 2000s, and especially for the SD group (Austria and Italy had high percentages early on in the 1960s). Similar development has not happened for the Northern donors, except for Belgium. Interesting is also the low activity on the sector during the 1980s for all three groups, and the increased activity in the 2000s. The growth of sector VII on total ODA in shares is an indication that debt–related practices are an active component in development cooperation.

5.2 Debt Practices

Loans, grants and debt relief given by the EU Member States to the developing nations is presented here in the following order: (1) Grants, loans and debt relief in sums, followed with by region data and by income data,(2) ACPs vs. non–ACPs in terms of given grants, loans and debt relief, (3) EU versus multilaterals in given grants, loans and debt relief.

5.2.1 Grants, Loans and Debt Relief

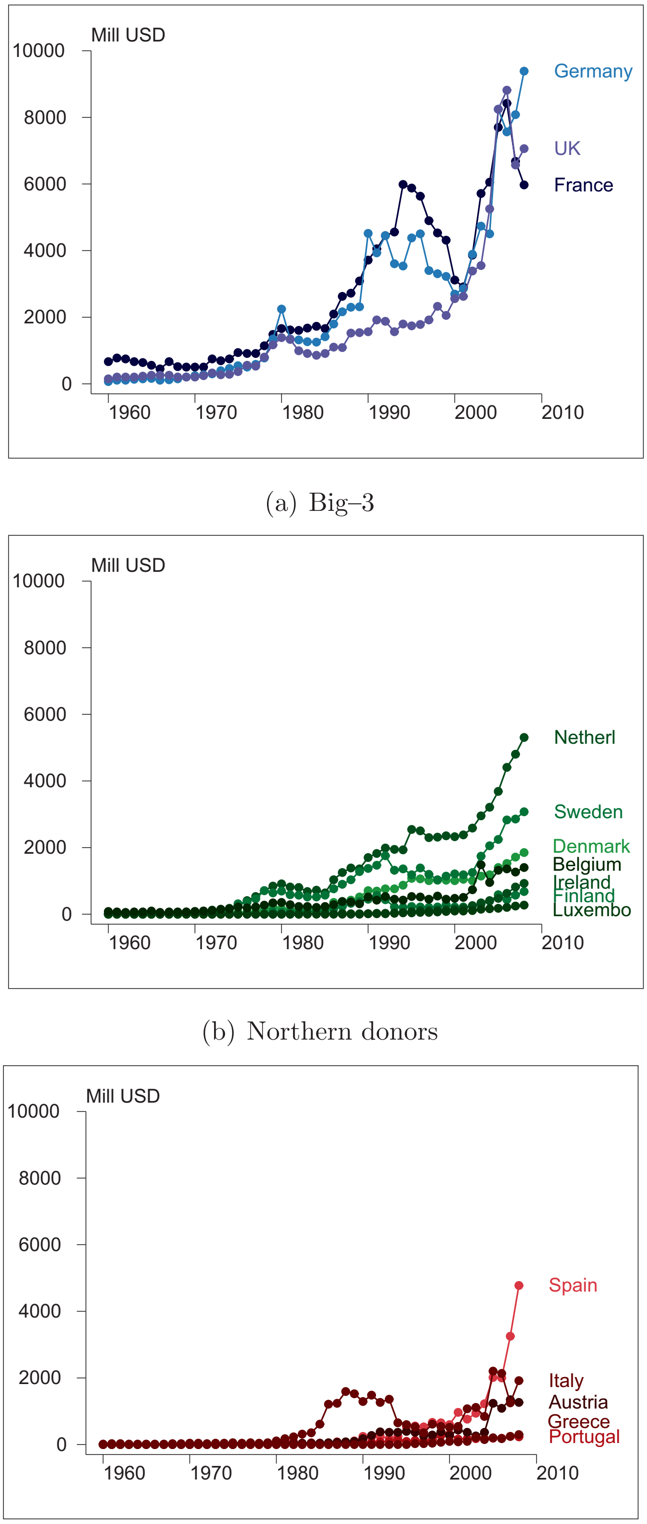
This chapter includes grants, loans and debt relief. Grants are included to provide a good backdrop to which loans and debt relief are to be compared to.

GRANTS

Grants to the developing nations have been reported in OECD DAC statistics since the year 1960. Figure 5.4 shows the sums given by each EU Member State. As can be seen from the data, the differences in sums for the donor groups are substantial. What is also evident and important, is that countries within groups appear to have been acting in a similar manner.

Grant sums of the Big–3 countries have developed similarly, except during the 1990s when France and Germany gave more than the UK. Sums have increased steadily since the 1960s, except for France and Germany during the latter half of the 1990s and late 2000s for the UK and France. Grant sums from the Northern donors have also steadily increased during the time period. Netherlands, Sweden and Denmark have given the most aid in sums out of the group. It is clear from figure 5.4 that the Northern countries have gotten a later start in their grants than the Big–3. Grant sums from the SDs are smaller when compared to the Big–3 countries. Like the NDs, the Southern donors have gotten a later start to grants,

Figure 5.4: Grants to the developing nations in sums



(a) Big–3

(b) Northern donors

(c) Southern donors

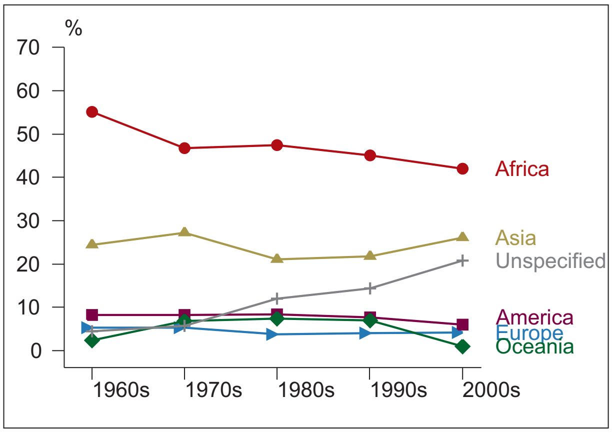
even later than the Northern countries. Italy has given larger sums in the late 1980s and early 1990s, but others started as late as early 1990s. Reasons for this have been overviewed in table 3.2. As the new millennium has approached, a all EU–15 countries have acted as donors. Overall when comparing the grant sums of the donors, it is noticed that (1) the timing for the start of giving grants is different for the donor groups, (2) there are differences between the stability of given sums, and

(3) countries in each donor group indicate similar developments in their grant sums during different times than the other countries in that same group.

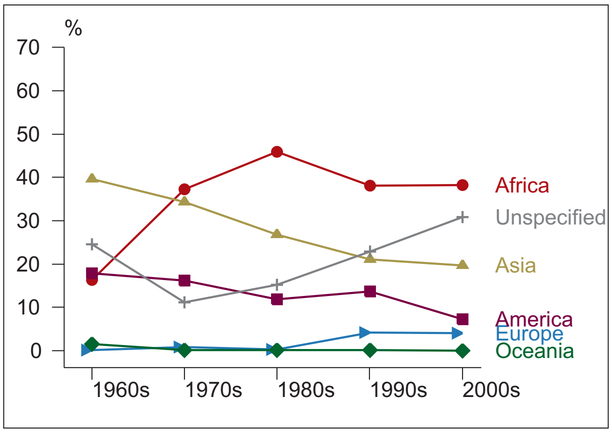
Grants by Region

Grants by region data presented in figure 5.5 shows the differences between the donor groups in the allocation of grants to the developing nations by regions.

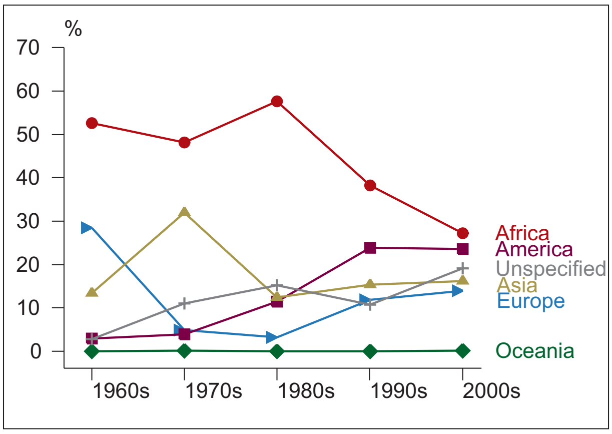
Figure 5.5: Grants by region from the three donor groups.



(a) Big–3



(b) Northern donors



(c) Southern donors

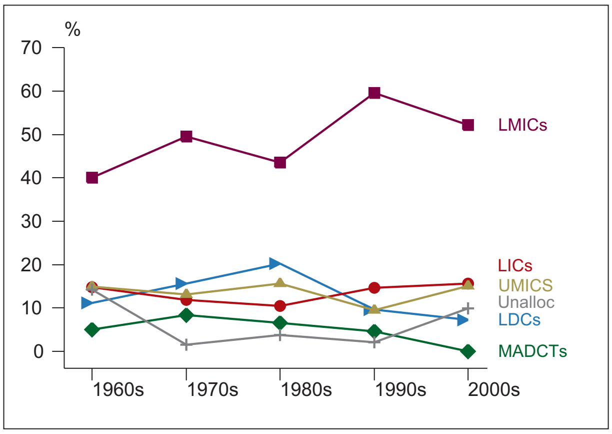
All groups share the overall increase in the percentage allocated to the Unspecified group. All groups have also given most aid throughout the time period to Africa. Least grants have been allocated to Oceania. Big–3 group has been fairly stable in its allocation and no large shifts have occurred, except for the rise in the shares allocated to the unspecified group and the slight decrease in grants going to Africa and Oceania. Northern donors have varied a bit more, Africa's share has risen during the early phases of ODA. Asia's share has decreased significantly towards the 2000s, America's share has also decreased, but not as much as Asia's share. Opposing developments have occurred in the cases of America (share of grants from the NDs decreased, share of grants from the SDs increased during the time period), and in the case of Africa (rapid decline in shares of grants from the SDs and the Big–3 during the 1960s, sharp increase in grants from the NDs during the same time). Also, Europe's share of grants is much higher from the Southern group than the other two donor groups. Looking at the main differences in the data concerning the 2000s, it is clear that America's role as a recipient of grants from the NDs and the Big–3 has decreased, but the Southern donors have allocated nearly as much to it as Africa. Southern donors overall show the most variation. Interestingly, Africa, America, Asia, Europe and the Unspecified groups are coming together in their share in the 2000s. While the two other groups indicate clear preferences towards some groups, such as Africa in the case of the Big–3 and the NDs, no such preference appears in the case of the Southern countries, or at least the differences among group shares are smaller. Policies towards grant allocation therefore seems to be more equal in the case of the Southern donors, while the Big–3 prefer Africa and Asia, and the Northern donors prefer Africa as well. This might be because of the lower grant sums, fairly short history of giving grants, and simply that there hasn't been enough time to form traditions concerning grant allocation. Low finances are also a possible cause for variation between annual sums.

Grants by Income

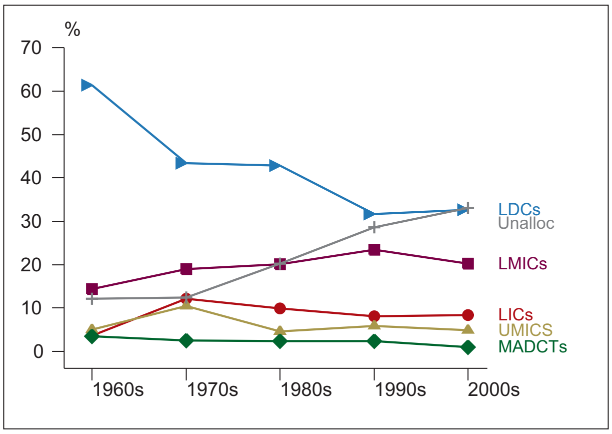
Grants by income data in figure 5.6 indicates which income groups have received the most grants from each of the three donor groups. Again, similar developments can be seen in this data than in the two previous data sets. The Big–3 group has shown stable policy throughout the time period; main focus of grants has clearly been the LMIC group, while other five groups have received much lower shares. Like the Big–3, the Northern donors have also preferred one group, but that group has been the LDC group, not the LMIC. This is a relevant difference in policy between the donors, which is somewhat expected based on the characteristics of development assistance.

The share of grants going to the LDCs have also decreased significantly during the time period, and in the 2000s the Northern donors have allocated same shares to the LDCs and the unallocated group. The Southern donors have again had the most variation between groups, and there is no clear policy pattern emerging from the data. Like in the case of the two other donor groups, grants going to the LDC group

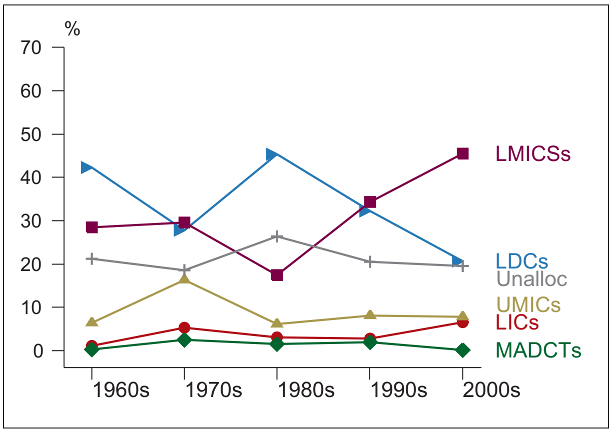
Figure 5.6: Grants by income from the three donor groups.



(a) Big–3



(b) Northern donors



(c) Southern donors

have decreased for the SDs as well since the 1980s. This development is somewhat unexpected as the role of the least developed/poorest developing nations has been emphasized both in EU documents and in global development discourse. What is expected however is the low share of grants allocated to the MADCT group from all three donor groups[3].

[3]MADCT countries are former developing countries

LOANS

Loans to the developing nations have also been reported in OECD DAC statistics since the 1960s. Loan sums for each donor are presented by group in figure 5.7. Germany and France have had a surprisingly similar development concerning loans sums. Surprising is UK's role in the 1980s and 1990s, when it has loaned significantly smaller sums, near to zero level, despite the fact that in the 1960s and 1970s countries indicated similar policies, and again in the 2000s when UK's sums have increased. Sums of the Northern donors are significantly smaller, largest sums have been loaned by the Netherlands and Denmark during the 1980s. The overall timing of loans is rather different than those of the Big–3's, peak time period for the Northern donor group was the late 1970s to early 1990s. Loans from France and Germany increased heavily during the entire 1980s and again in the early 2000s when also UK has given larger sums. Sums loaned by the Southern donors are mainly from Italy and Spain. What is surprising here is that the sums of loans have in fact increased after the debt crisis. Peak time for loans was early 1990s, a decade after the debt crisis. The given sums also vary more than for the other donor groups.

Overall when comparing the sums of loans by the three groups the main differences concern (1) the timing of given loan sums, and (2) the differing reactions after the debt crisis. Peak timing for loans for the Big–3 was in early 1990s and again in the 2000s, for the NDs it was during late 1970s to early 1990s and for the Southern donors the late 1980s and early 1990s. As the Northern donors have reduced their already small sums given in the 1980s, the Southern donors have in fact increased theirs after the debt crisis. Big–3 group donors France and Germany have also decreased their shares, but UK has increased its sums in the 2000s, approaching the sums of France and Germany. What is also notable in the data is that the decreasing of the sums, by the Big–3 for example has happened mainly in the 1990s, fairly late after the beginning of the debt crisis. In the late 2000s, France, Germany, UK, Spain have increased their loans sums, surpassing the annual sums given before the debt crisis.

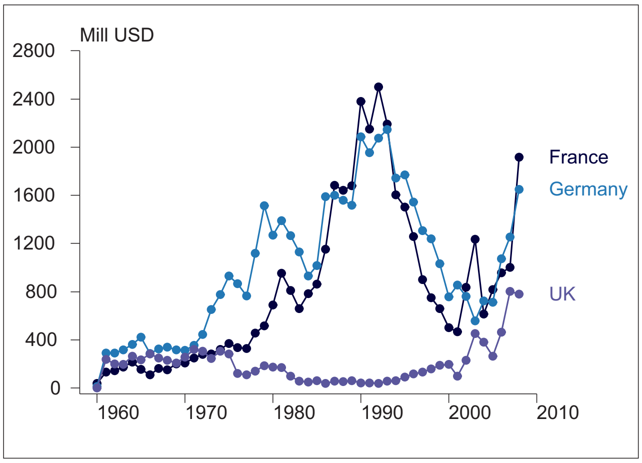
The relative impact of the differing policies between the donor groups should be analyzed while keeping the large differences of sums in mind, i.e. good policies of the NDs do not really matter if the sums given by them are many times smaller than those of the two other groups.

Loans by Region

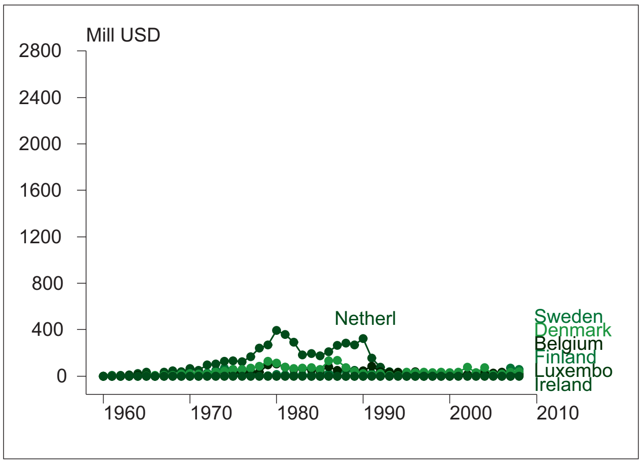
Loans by region data for the three donor groups is presented in figure 5.8. This data indicates some similar developments previously seen in the grants by region data, for example concerning the role of America.

Overall the three donor groups appear of having largely differing histories of allocating loans to the developing nations. Big–3 countries appear to have been practicing a common policy, where mainly loans have been allocated to Asia and

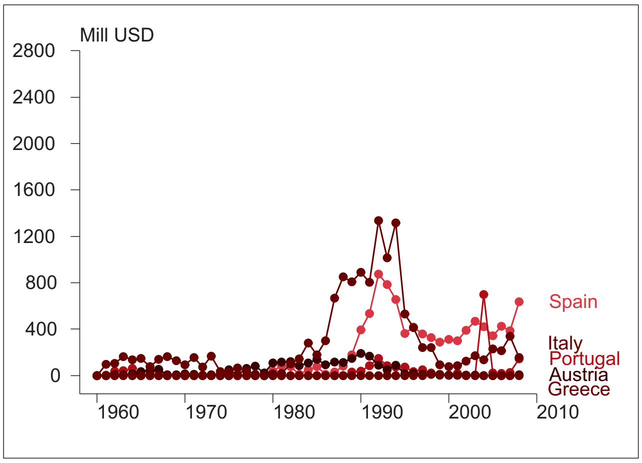
Figure 5.7: Loans to the developing nations in sums



(a) Big–3



(b) Northern donors



(c) Southern donors

Africa, while the other three groups and the unspecified group have gotten much less, America and Europe about both 10%, unspecified and Oceania near 0%. Northern donors on the other hand have varied more in their loan share allocation. Clearly most loans have gone throughout the time period to Asia, Africa coming in second, but with much lower shares. America was given almost as much loans in the 1960s, but the shares have lowered during all decades, stabilizing to about 10% in the

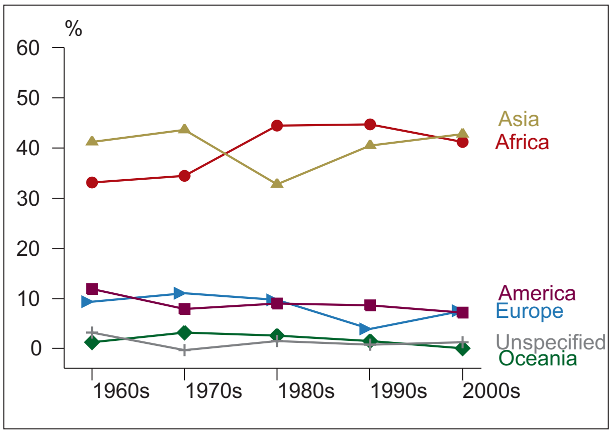
1990s and the 2000s. NDs also prefer Asia and Africa as the main recipients of loans, but the differences between these groups are larger than in the case of the Big–3. Southern donors on the other hand have had the most variation in their loan shares. Africa has been the main recipient of loans. As in the case of grants to America, also loan shares from the SDs to America have increased during the 1970s and the 1980s. While the Big–3 and the NDs have allocated very little loans to America, SDs still give about one–fourth of its loans in the 2000s to that region. All groups have allocated the least loans to Oceania. Largest allocation to the unspecified group in the 2000s has been given by the NDs.

Overall the most important differences among groups in terms of loan allocation is that the Big–3 seem to have been practicing a set policy during the entire time period, or at least their shares have changed the least. NDs have clearly reacted to happenings in the debt field, for example by lowering America's share of loans and by favoring Asia in its loan allocation. SDs have practiced a widely varying policy, where shares have changed significantly and not to a favorable direction. In order to find out more specifically to which income groups these loans have been given to, data by income is presented next.

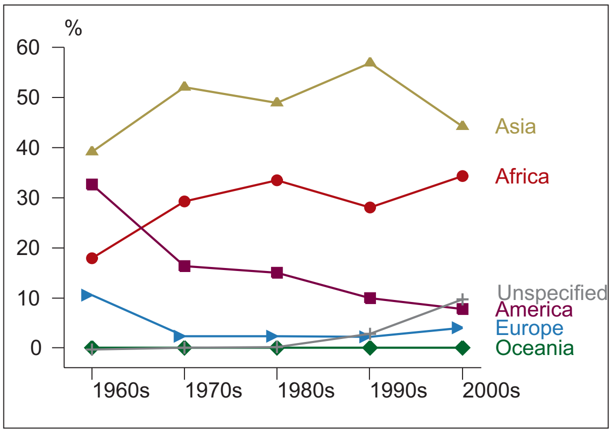
Loans by Income

Loans by income data shows which income groups have received loans from each donor group. Loans by income data reveals that all three donor groups have similar policies concerning loan allocation, but some differences do occur. All three groups have allocated most loans throughout the time period to the LMIC group. Share of loans going to the LMIC have increased steadily since the 1960s. Based on previously presented knowledge concerning how loans function (successfully), this policy is useful. The Big–3 countries have given similar, much lower sums to other groups, with very little variation. The NDs have had more variation than the Big–3 group, but not as much as, again, the SDs. In the 2000s, the groups receiving the second and third most loans were the LICs and the UMICs from the Big–3, the LDCs and the LICs from the NDs, and the LDCs and UMICs from the SDs.

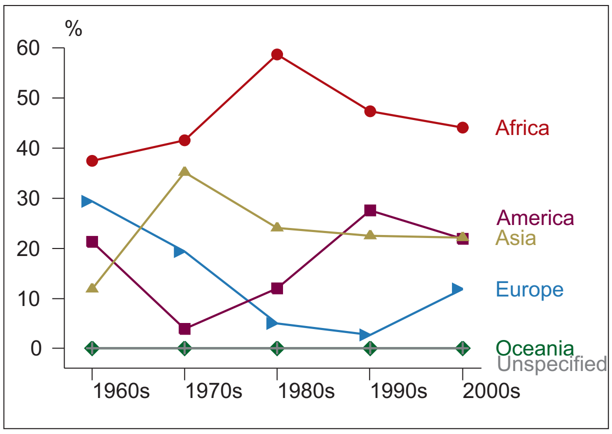
Figure 5.8: Loans by region from the three donor groups.



(a) Big–3

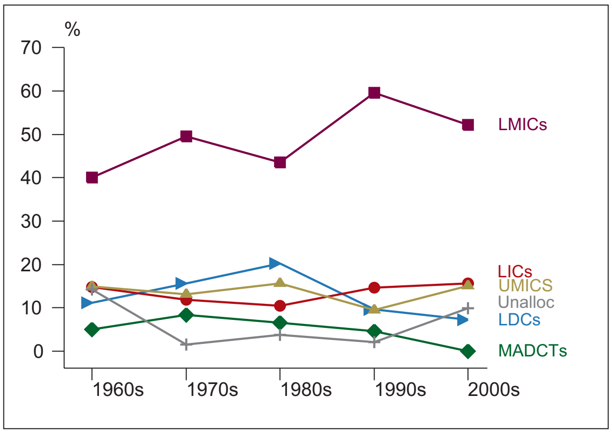


(b) Northern donors

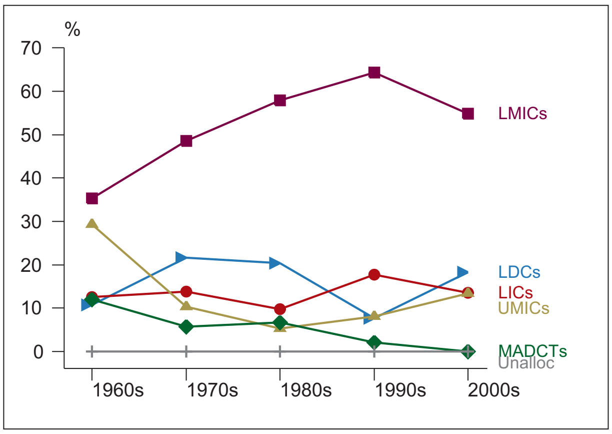


(c) Southern donors

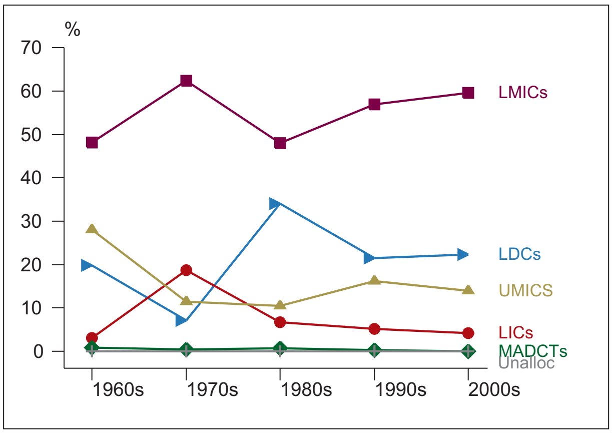
Figure 5.9: Loans by income from the three donor groups.



(a) Big–3



(b) Northern donors



(c) Southern donors

The most important similarities in the loans by income data is that all groups have allocated the largest shares of loans to the same income group. Variation has again been the highest in the case of the SD group. One important difference is the larger share of loans allocated to the LDCs by the SDs especially during the 1980s when nearly 40% of loans were given to the poorest developing nations by the SDs.

DEBT RELIEF

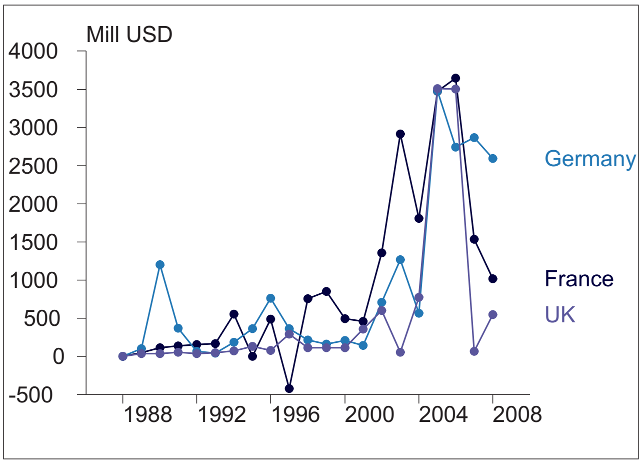
Debt relief has been reported in OECD DAC since the year 1988, approximately five years after the beginning of the debt crisis. On the basis of data in figure 5.10 it is observable that the largest sums have been given in the 2000s.

Interestingly, although debt relief started in 1988, sums have been multiple times larger in the 2000s for all donors. Debt relief sums should also be scaled to loan sums presented before, i.e. how much has been lent affects those sums which can overall be forgiven (for example Northern donors versus the Big–3). Ireland and Luxembourg have not given debt relief at all, but also not loans either. Southern Donors started giving debt relief three to five years later than other donors, as late as mid–1990s (with the exception of Greece). Large annual sums in 2005 are mostly due to the Tsunami of December 2004; and loan forgiveness for Iraq during the Iraq War (in 2005 and 2006).

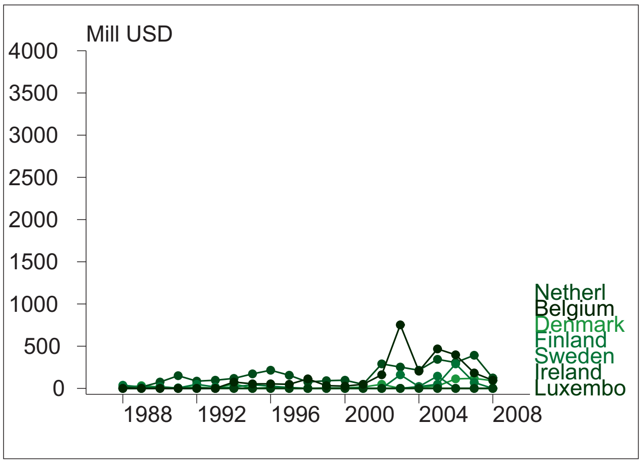
Since debt relief is already included in the grant statistics, the shares going to different regions and income groups are presented here in table format. The data includes mean debt relief for 1980s, 1990s and 2000s[4]. Debt relief data by region and income is presented in means and using the Coefficient of Variation (CV=[standard deviation/mean]*100). This gives a percentage sum, indicating how big the variation of each donor group's debt relief. For example, if CV is 300%, variation is three times as large as the mean, indicating very strong differences in annual data. If CV is about 20%, it would be an indication that the variation is very low, i.e. policy concerning allocation of funds would in that case be fairly stable. In the data concerning region, it is clearly seen which regions did not receive debt relief at all (means=0, and CV=0), these regions were Europe, America, Unspecified and Oceania in the 1980s. Main recipients of debt relief were Africa and Asia, and mainly by the Big–3 and the ND groups. During the 1990s, activity rose for all groups. All groups got the highest means in the 2000s, during which more debt relief has been given, as was seen in figure 5.10. The coefficient variation measure for the data indicates that during the 1980s NDs and the SDs had the lowest variation, while the Big–3 had most fluctuation. During the 1990s the NDs had the lowest CV in general, while the SDs and the Big–3 fluctuated more. During the 2000s less variation occurred in all groups when compared to the 1990s. This might be an indication of that debt relief practices have stabilized. It is also noted from data

[4]The 1980s data of course includes only the years 1988 and 1989, so it should be taken into consideration that the means and Coefficient of Variation have been calculated for only two years in that case.

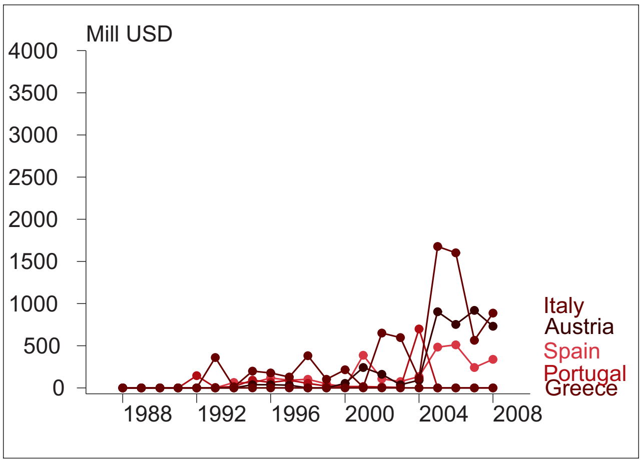
Figure 5.10: Debt relief to the developing nations in sums.



(a) Big–3



(b) Northern donors



(c) Southern donors

that groups receiving low means also often have high CV, this is an indication that country groups receiving little debt relief should be prepared that it is not allocated as stable as for regions receiving lots of aid with low CV, such as Africa in the 1990s for the SDs (mean 220 millions of USD, CV 71%), and Oceania in the 2000s (mean 2.72 millions of USD, CV 300%).

Debt relief by income data revels similar results. What is particularly worth

Table 5.1: Debt relief by region, donor groups.

Group	Measure	Europe	Africa	America	Asia	Oceania	Unspec
Big–3							
1988–1989	Mean	0	90.16	0	7.50	0.01	0
	CV	0	137.11	0	141.42	141.42	0
1990–1999	Mean	14.69	614.83	97.00	28.01	0.10	0
	CV	275.78	67.95	138.05	84.55	340.90	0
2000–2008	Mean	195.62	2939.85	89.16	1311.79	0.03	1.27
	CV	161.80	90.25	125.61	112.49	265.96	300.0
Northern							
1988–1989	Mean	0	72.53	0	1.75	0	0
	CV	0	1.59	0	51.46	0	0
1990–1999	Mean	3.31	88.97	52.19	43.33	0	13.64
	CV	197.06	39.44	70.42	107.64	0	168.03
2000–2008	Mean	18.57	466.56	11.87	132.12	0	4.08
	CV	177.63	81.03	103.86	130.83	0	198.74
Southern							
1988–1989	Mean	0	0.49	0	0	0	0
	CV	0	80.81	0	0	0	0
1990–1999	Mean	0.10	220.63	23.71	6.22	0	0.69
	CV	316.23	71.47	166.88	191.09	0	276.74
2000–2008	Mean	40.72	663.11	160.93	614.02	2.72	0.20
	CV	153.04	71.47	90.67	126.16	300.00	197.35

Table 5.2: Debt relief by income, donor groups.

Group	Measure	LDC	LIC	LMIC	UMIC	MADCT	Unalloc
Big–3							
1988–1999	Mean	82.70	8.76	3.86	0.94	0	1.42
	CV	141.42	141.42	141.42	141.42	0.00	133.43
1990–1999	Mean	324.39	130.19	280.82	10.48	0.33	8.42
	CV	59.52	144.31	97.25	234.90	316.23	315.86
2000–2008	Mean	853.31	1473.49	1964.49	245.08	0	1.35
	CV	96.20	170.58	93.60	133.97	0	280.81
Northern							
1988–1989	Mean	45.58	54.04	0.38	0	0	0
	CV	2.10	0.79	141.42	0	0	0
1990–1999	Mean	19.97	42.81	29.24	3.14	0	4.85
	CV	39.10	31.50	53.43	89.23	0	163.07
2000–2008	Mean	17.27	53.52	26.81	2.29	0	0.11
	CV	59.89	27.68	70.81	162.88	0	300.0
Southern							
1988–1989	Mean	0.49	0	0	0	0	0
	CV	80.81	0	0	0	0	0
1990–1999	Mean	176.47	17.85	52.11	4.13	0.10	0.69
	CV	85.13	159.88	148.77	215.63	316.23	276.74
2000–2008	Mean	317.27	214.84	908.11	41.28	0	0.20
	CV	92.65	148.41	92.70	171.75	0	197.35

noticing here is for example the allocation of debt relief to the LDC, LIC, LMIC and UMIC, which all have the same CV value in the 1980s. This may appear a be mistake in data, but it is in fact not. This indicates that some regular policy and a a clear pattern did exist during that time. Otherwise, the data reveals that CV values during the 1980s were highest for the Big–3, and lowest for the SD as they did not give much debt relief during that time. During the 1990s highest CV values are gotten by the SDs. During the 2000s, donor groups receive similar CV values, but Northern donors have the least variation in allocation to all income groups, except in the case of unallocated group.

Next, the differences between ACPs and non–ACPs are compared in terms of loans, grants and debt relief. The special role of ACPs in EU development policy history has been discussed in this study, and the aim of the next chapter it to describe how this special role is seen in the statistics.

5.2.2 ACPs vs. non–ACPs

The role of the ACPs and the non–ACPs has been special in EU development policy throughout the time period it has existed. Here, the role of the two groups is compared in terms of differences in the given grant, loan and debt relief shares. For the debt policy to be "mathematically equal", the sizes of the country groups are to be compared. (Note here that it is widely known that mathematically equal policy in EU politics is not possible or even desirable, but for the sake of argument the groups are compared in these terms.) Since the ACP group includes 71 countries[5], and the non–ACP includes 100 countries, the non–ACPs are approximately 60% of the total group ([100/171]*100=58.5%).

Figure 5.11 shows the shares of allocated loans and grants to the non–ACPs. The 60% line is drawn to the diagram to indicate where the values should be in order for the policy to be "equal".

Grant shares to the non–ACPs have in fact been approx. 60% since mid–1960s to 2000s. In the first years share was over 80% and again in the late 2000s it was about 70%, but the general level has been at about 60%. Loan shares to the non–ACP group on the other hand have varied between 100% in 1960 to 80% in the 1960s and 1970s to about 60% in late 1980s, and again nearly 90% in the 2008. According to this data, more loans have been allocated to the group than should be considering the size of two groups and if these groups were to be treated as equals.

Share of debt relief to the non–ACPs and ACPs presented in figure 5.12 has

[5]This data includes those 71 states the OECD names as ACPs in their data. In the EU ACP information page there are overall 79 ACPs named. Countries included in the data are: Angola, Benin, Botswana, Burkina Faso, Burundi, Cameroon, Cape Verde, Central African Rep., Chad, Comoros, Congo, Dem. Rep., Congo, Rep., Cote d'Ivoire, Djibouti, Equatorial Guinea, Eritrea, Ethiopia, Gabon, Gambia, Ghana, Guinea, Guinea–Bissau, Kenya, Lesotho, Liberia, Madagascar, Malawi, Mali, Mauritania, Mauritius, Mozambique, Namibia, Niger, Nigeria, Rwanda, Sao Tome & Principe, Senegal, Seychelles, Sierra Leone, Somalia, Sudan, Swaziland, Tanzania, Togo, Uganda, Zambia, Zimbabwe, Antigua and Barbuda, Bahamas, Barbados, Belize, Dominica, Dominican Republic, Grenada, Haiti, Jamaica, St. Kitts–Nevis, St. Lucia, St.Vincent & Grenadines, Trinidad and Tobago, Guyana, Suriname, Fiji, Kiribati, Papua New Guinea, Samoa, Solomon Islands, Tonga, Tuvalu, Vanuatu. (OECD DAC Statistics portal)

Figure 5.11: Loans and grants to the non–ACPs.

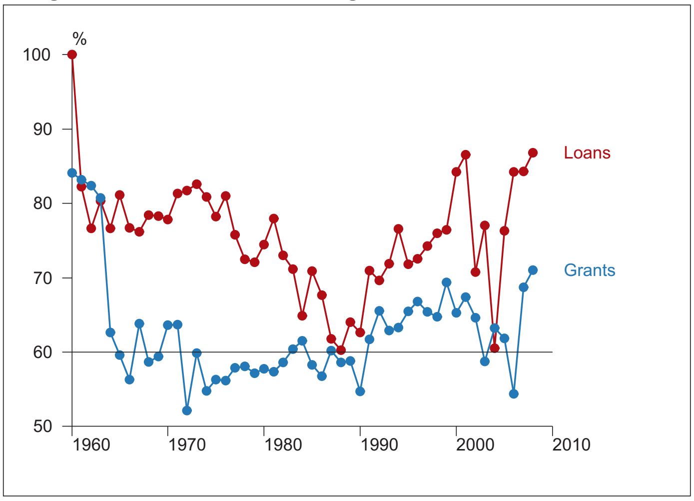
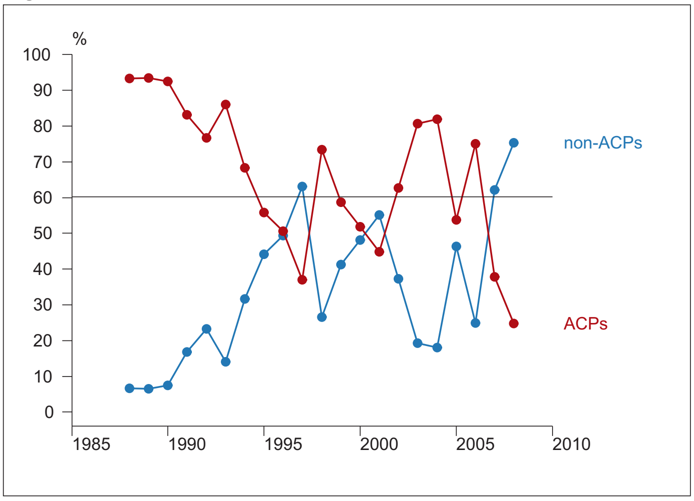


Figure 5.12: Debt relief to the ACPs and non–ACPs

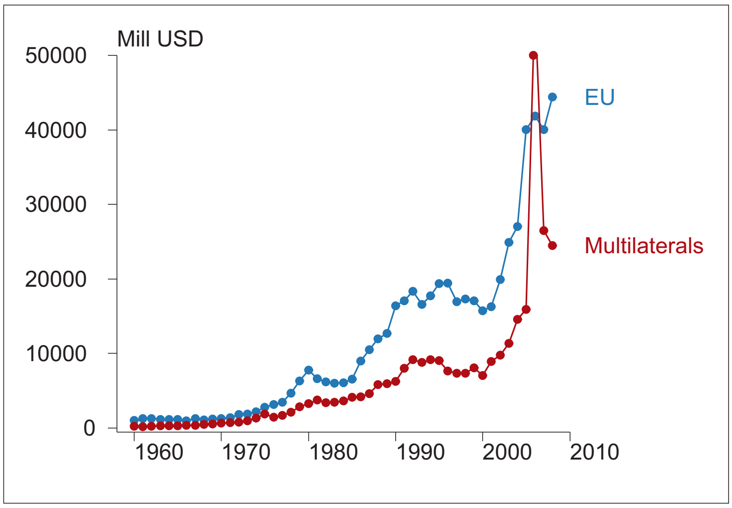


varied significantly. In the late 1980s over 90% went to the ACPs, and very little to the non–ACPs. The development, or ”coming together” of the shares going to the groups in 1988–1996 is very interesting. Despite differing group sizes, only on three occasions has the level of debt relief for non–ACPs exceeded the ACPs; in 1997 at 63%, in 2001 at 55%, and in 2008 at 75%. Data indicates that the ACPs have gotten more debt relief than they should have based on their group size. However, this might be due to the fact that more loans have been given to this group as well. Next, the practices of the EU countries are compared to those of the multilaterals.

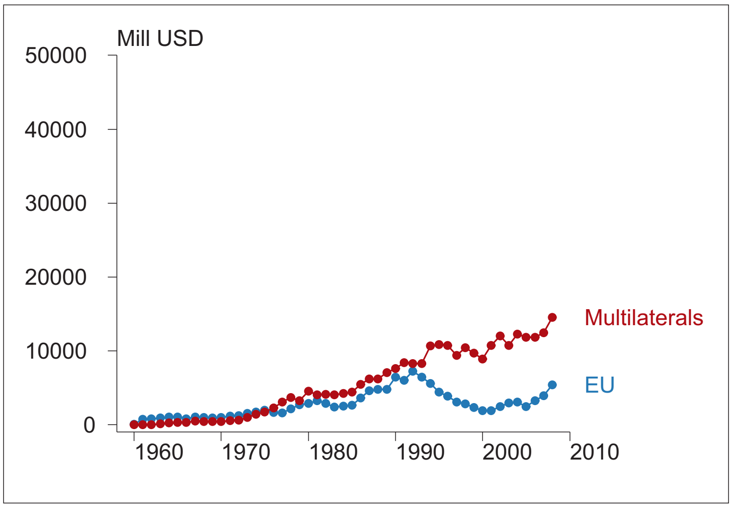
5.2.3 EU vs. Multilaterals

The main focus of this study is on the differences between Member States in giving different kinds of ODA. It is however also important to know how the EU–15 countries as one compare to the multilateral organizations. The data presented here includes the OECD DAC EU Member States and 28 multilaterals. Since EU Member states also fund the multilaterals through the ODA system, the presented data is partially overlapping. Multilaterals include also EU institutions and the Council of Europe. Other organizations included are AfDB, AfDF, AsDF, CarDB, Council of Europe, EBRD, EU Institutions, GAVI, GEF, Global Fund, IBRD, IDA, IDA Sp.Fund, IFAD, IFC, IMF, IMF Trust Fund, Montreal Protocol, Nordic Development Fund, UNAIDS, UNDP, UNECE, UNFPA, UNHCR, UNICEF, UNTA, WFP and Arab Agencies.

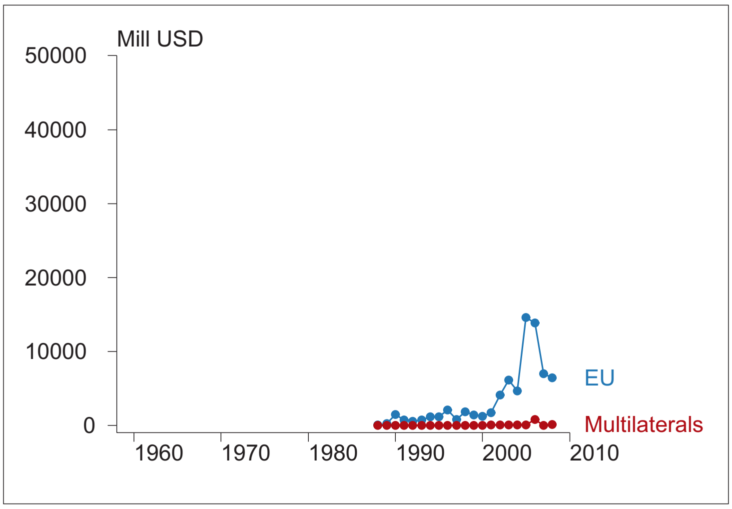
Figure 5.13: EU versus multilaterals: grants, loans and debt relief sums.



(a) Grants



(b) Loans



(c) Debt relief

Given grant sums for the two groups are highly similar, EU Member States have given combined a bit more (except in 2006) and both sums have increased towards the 2000s. Sums have been similar particularly during the earliest time period under focus, the 1960s, 1970s and 1980s.

Loans from the EU Member States and the Multilaterals are quite interesting. Initially EU gave more loans than the multilaterals, but this changed already in early 1970s. Since then up until early 1990s, sums have increased for both. In 1992 loans from the EU started decreasing but the multilaterals' loans kept increasing. Loans sums have increased again in the late 2000s for the EU Member States as well. Year 1992 marks an important policy shift in loans practices. The cause of this policy shift should be further explored.

The data concerning the relationship of debt relief given by the EU Member States and the multilaterals reveals a dramatic difference in volumes of debt relief. This is however expected as the multilaterals do not mainly give debt relief. When a country gives debt relief for example within the HIPC initiative that debt relief appears in the bilateral statistics, not as multilateral debt relief. In these terms the data used does give a slightly wrong impression of the involvement of the multilaterals in debt relief initiatives, which has been brought up in previous chapters.

The final part of this study applies partially the data presented in the previous parts of this chapter to measure the current orientation of ODA of each EU–15 Member State.

5.3 Grant–Loan Index

The Grant–Loan Index developed here is an example of a possible use of the data examined in this study. It is developed to test how the data used can be applied to gain more concrete knowledge of the characteristics of each Member State in terms of their ODA structure. The Grant – Loan Index aims to portray the differences among EU Member States between ODA practices in a concrete manner, focusing on the division between loan aid and grant aid. Results of the comparison are compared to the EU Member State division by Carbone (2007a) and they will also be presented using Chernoff (1973) method of visualizing data with faces.

Data used is obtained from OECD DAC statistics portal, as mentioned, and will include ODA grants and ODA loans from the years 2000–2008. This time period was chosen for different reasons; first of all, the data is current and therefore relevant "today". The time period is long enough to do some meaningful comparison between Member States, and all Member States included have been EU Members for several years before the year 2000 (at least 5 years). Also, the 2000s are considered of being a separate time period in EU development policy during which several important agreements have been signed, including the Cotonou agreement in 2000, the MDGs in 2000 and the Consensus in 2005, see for example (Carbone, 2008, pg. 58) or (van

Reisen, 2007, pg. 56–58).

5.3.1 Idea

My idea to develop and use an Index for this data started with a notion that there is a large amount of data available concerning the issue and finding the most relevant points, similarities and/or disparities, is quite a challenge to anyone who is not familiar with the data beforehand. The index formed here is merely one way of approaching the issue and comparing the countries to each other. The spirit of debt practices data analysis has been hypothesis generating; therefore this Index is to be interpreted as one example of the use of this data to form a new approach to looking at the behavior of the EU Member States.

The results of the Index are compared to Carbone's (2007a) group division. However, the variables used in this index are entirely different from those used by Carbone. Carbone's data concerned mainly the quality of ODA, this comparison will concern mostly the structure of ODA. Carbone's study yielded the model which included three different donor groups to which the EU Member States were divided to; the Big–3, Northern and Southern donors. Each of these groups had different typical characteristics Carbone had concluded on the basis of the data he used. Carbone concludes the Northern donors as being the best performers of development assistance in terms of both, quality and quantity. They have a strong tradition of church missionary work and are mainly motivated and driven by idealistic reasons. (Carbone, 2007a, pg. 46) SDs have not had a far–reaching tradition of development cooperation, and all but Italy have become donors relatively late. Aid allocation has been driven by colonial heritage. In many cases internal political crises have reduced aid. France and UK have both maintained close relations with their colonies, but Germany has not favored any geographic area over others. All have acted as significant donors, in Germany's case aid has been driven by commercial reasons as well. France has suspended aid for human right's violations, and UK was the first to use conditionality to aid. (Carbone, 2007a, pg. 41–47)

In this comparison, Northern donors are hypothesized to be mainly grant oriented in their practices since they've had a strong moral element in aid since its beginning. Northern donors' development aid history as church missionaries speaks for favoring grant–type forms of assistance. They are also the best performers in aid (quality and quantity) according to Carbone, which is important here. The Big–3 group is hypothesized as being both "loan and grant oriented". This is based on the fact that they all have given high volumes of aid, but also have had stronger commercial components in it (for example Germany). High shares of aid have gone through the EC, so readiness for multilateral cooperation and loans as well do exist. They also have both extensive colonial histories (including far–reaching traditions of giving loans), and also substantial financial means available for different kinds of ODA. Southern donors are hypothesized to be mostly loan oriented in their practices as some of them have had strong colonial legacies and tradition of giving loans from

Table 5.3: Grant – Loan Index variables and description.

Variable	Description
Grants by Income in % of ODA (GI)	Mean of grants allocated to the LDC and LIC groups in ODA. The higher the share of grants given to the poorest two country groups, the more points the country receives.
Loans by Income in % of ODA (LI)	Mean of loans allocated to the LDC and LIC groups in ODA. The higher the share of loans given to the poorest country groups, the less points the country receives.
Loans in % of Grants (LG)	Mean of loans in grants ([loans/grants]*100). The higher the share of this percentage, more loan–oriented the country is and the less point it receives.
ODA in % of GNI (OG)	Mean of ODA in GNI. The higher the share of ODA in GNI, more points the country receives.
Grants , CV, (VG)	Variation for grants is measured by using the Coefficient of Variation ([standard deviation of grants/mean of grants]*100). The higher the variation is, less points the country receives since the higher the variation, the less predictable the given ODA is. Note! CV can be over 100%.
Loans, CV, (VL)	Similarly with "Grants, CV", more variation, less points the country receives.

early on. They've also had political crises' in the recent years, which have affected annual ODA sums and their lower GDP per capita could also induce giving loans as they provide a way to accumulate some wealth through interest rates (Carbone, 2007a, pg. 41–47)

5.3.2 Composition

The developed Index formed in this study includes six different variables; (1) Grants by Income (GI), (2) Loans by Income (LI), (3) Loans in per cent of grants (LG), (4) ODA in per cent of GNI (OG), (5) Variation of Grants (VG) and (6) Variation of loans (VL). The formation of these variables is explained in table 5.3.

The Index rewards for giving grants to the two poorest income group countries, giving loans to the high income developing nations, of having a small share of loans in total grants, giving a large percentage of GNI as ODA and having a low amount of variation in both annual grant and loan sums. Low variation is rewarded as it indicates stable and well–thought of actions in the field of development. High variation of ODA sums, whether they are grants or loans, indicates vice versa that the system is perhaps not working as efficiently and rationally as possible, or that at least it is prone for fast and / or unpredictable changes. Fluctuations in annual support sums can also cause problems in the developing nations.

The countries received points between (minimum) 0 and (maximum) 20, for each variable, based on the values received. When the number for each country is calculated for a variable, the countries are then organized in order. The first three countries receiving for example the lowest share of ODA in GNI are given 0 points, the next three 5 points, next three 10 points, and the next three 15 points. The three countries with the highest points, receive 20 points. This is done for all six variables and always the EU Member States are compared to each other (not for example to how well each Member State is approaching the goals set for example in the MDGs). Comparison in order was chosen as the method since the main idea of this index is to compare the Member States to each other, not to their common goals, for example (goal was to describe structure of ODA, not outcomes or quality of aid). Comparing EU Member States actions to their goals would be almost meaningless when researching policy differences, since it is now known that nearly all EU Member States are in fact lagging behind on their development policy goals (mainly explained due to reasons concerning the recession starting in 2008), as was discussed earlier in chapter four. The Grant–Loan Index is based on a point system, and therefore it is possible for a country to receive same point accumulation although the policies differ. To overcome this challenge, I will use Chernoff's (1973) method of faces to portray visually the differences among the Member States. This method will aid in finding and understanding differences between the actors involved.

Table 5.4: Grant – Loan Index variable values.

Country	GI	LI	LG	OG	VG	VL
Austria	19.53	58.08	0.23	0.35	64.43	218.92
Belgium	48.67	51.78	2.35	0.46	37.72	145.93
Denmark	54.85	12.03	3.13	0.89	23.92	127.56
Finland	39.57	21.6	2.64	0.38	42.54	85.95
France	39.01	32.83	17.15	0.39	34.68	60.90
Germany	30.70	10.84	17.91	0.32	44.10	60.67
Greece	9.83	0	0	0.18	42.56	48.48
Ireland	66.53	0	0	0.43	58.39	48.11
Italy	40.95	29.19	14.17	0.19	50.16	45.65
Luxembourg	44.63	0	0	0.83	36.64	40.12
Netherlands	36.64	2.56	0.13	0.80	31.19	36.94
Portugal	64.99	75.08	103.78	0.28	22.92	24.91
Spain	17.98	12.46	31.15	0.30	75.18	0
Sweden	33.44	15.48	1.24	0.87	36.58	0
UK	52.21	27.4	7.76	0.38	45.42	0

Table 5.5: Grant – Loan Index points.

Country	GI	LI	LG	OG	VG	VL	Sum
Austria	0	0	15	5	0	0	20
Belgium	15	0	10	15	10	10	60
Denmark	20	15	10	20	20	5	90
Finland	10	10	10	10	10	15	65
France	10	5	5	10	15	10	55
Germany	5	15	0	5	5	15	45
Greece	0	20	20	0	10	20	70
Ireland	20	20	20	15	0	20	95
Italy	10	5	5	0	5	10	35
Luxembourg	15	20	20	20	15	20	110
Netherlands	5	15	15	15	20	0	70
Portugal	20	0	0	0	20	0	40
Spain	0	10	0	5	0	15	30
Sweden	5	10	15	20	15	5	70
UK	15	5	5	10	5	5	45

5.3.3 Results

The results of the Grant – Loan Index reveal interesting issues concerning the EU Member States' policy differences. Points received by each Member State are listed in table 5.4 by variables and by corresponding index points in table 5.5.

Since differing policies can yield similar results in this Index (points counted together), it is important to know exactly how the policies differ. Due to this, data for the index is summarized, including each variable and the points each country has received for it.

The minimum and maximum values in each variable case indicate more specifically what kind of differences there are between the Member States. In the case of variable "Grants by Income", which was "how large percentage (%) of grants in ODA on average have gone to the two poorest country groups during the years 2000–2008", Ireland gave nearly 70% and Greece less than 10% on average. Similarly, in the "Loans by Income" variable, Portugal gave over 75% on average of its loans to the two poorest country groups LDC and LIC, whilst some of the Northern donors gave something closer to 10–20%, and some did not give loans at all. Share of loans in aid varied between 0% (or close to 0%) to over 100% (103.78% for Portugal, meaning that they gave more loans than grants on average). Northern donors have had constant low shares of loans in grants.

Share of ODA in GNI in (%) varies between 0.18% (Greece) to 0.89% (Denmark). Coefficient of Variation of grants and loans indicate also interesting differences. The lowest Coefficient of Variation of grants is Portugal (22.9%), i.e. that Portugal has varied the least out of all EU Member States in the amounts of grants it has allocated to the developing nations. Interestingly, Portugal also has the highest Coefficient of Variation for loans, over 200%. Meaning that its loans amounts have varied the most in comparison to other EU Member States, and that variation has been quite substantial, over double. Similar kind of case is Spain, which has the highest Coefficient of Variation of grants, but the lowest Coefficient of Variation of loans (24.9%, out of countries which have given loans). It is really important to note also that on average the EU Member States have much higher variation in their loan sums than in their grant sums. The mean for grant Coefficient of Variation for the data presented in table 5.4 is approximately 43%, and approximately 63% for loans. As can be seen from the data in the same table, some EU Member States have low variation of grants, and high variation of loans, such as Austria, Denmark, Netherlands, Sweden, UK and the previously mentioned Portugal. Some Member States had less of a difference between the variation (still higher variation for loans than grants), such as Belgium, Germany and Italy. Only two countries had more variation in grants than in loans, which were Finland and Spain.

The overall order of the countries is presented in table 5.6. Grant–Loan Index results are in compliance with Carbone's model. The order between the EU–15 countries is mainly the same as in Carbone's division. Northern donors receive highest scores, Big 3 are placed in the middle and Southern donors received the least points. Exception is Greece, which received 70 points, and is therefore placed as high as Northern donors.

In order to understand the differences between the data, method of visualization called Chernoff's faces is used in the final part of this chapter.

Chernoff's Faces

Data visualization is always a challenge when dealing with multivariate phenomena such as in the case of the Grant – Loan Index. The chosen visualization method in this case needs to be able to portray key differences within a large group of countries in a manner, which is visually clear to readers. Normal diagrams or charts do not include options suitable for this. The point system used in this study included six variables; therefore there are multiple different ways of receiving same point total. The countries receiving low points did not have similar "bad" policies. If not visually

Table 5.6: Grant – Loan Index results.

Country	Total Points	Group
Luxembourg	110	ND
Ireland	95	ND
Denmark	90	ND
Netherlands	70	ND
Sweden	70	ND
Greece	70	SD
Finland	65	ND
Belgium	60	ND
France	55	Big–3
Germany	45	Big–3
UK	45	Big–3
Portugal	40	SD
Italy	35	SD
Spain	30	SD
Austria	20	SD

compared, it would be easy to bypass important policy differences.

As explained, the Grant–Loan Index uses ordinal scale, as values are given corresponding points in order and scaled to each other. But the visual comparison done here is for the original data, which includes ratio measurements. This assures that differences between the visual images are based on real and accurate data.

Chernoff's faces (1973) is a method of data visualization which fulfills the criteria in this case. It is a method which summarizes multivariate data subject to strong but possibly complex relationship in such a way that the investigator can quickly comprehend relevant information and then apply appropriate statistical analysis. (Chernoff, 1973, pg. 361) This type of data is used in the Grant – Loan Index, and the method is applied to create an actual a face for each Member State; each face represents that country's policy. The facial expression itself embodies how well or how poorly that country scored in the Grant – Loan Index, for example a smiling or content looking face means that country scored well, and grumpy or sad looking face means that it did not do so well in the comparison. The facial expression of each Member States' face is to be compared to that of the others. It is important to compare which countries have similar expressions, meaning that their Grant – Loan orientation is also similar. By focusing on the differences between facial expressions in figure 5.15 and the variables of the Grant – Loan Index is table 5.4, it is possible to notice where differences occur in policies.

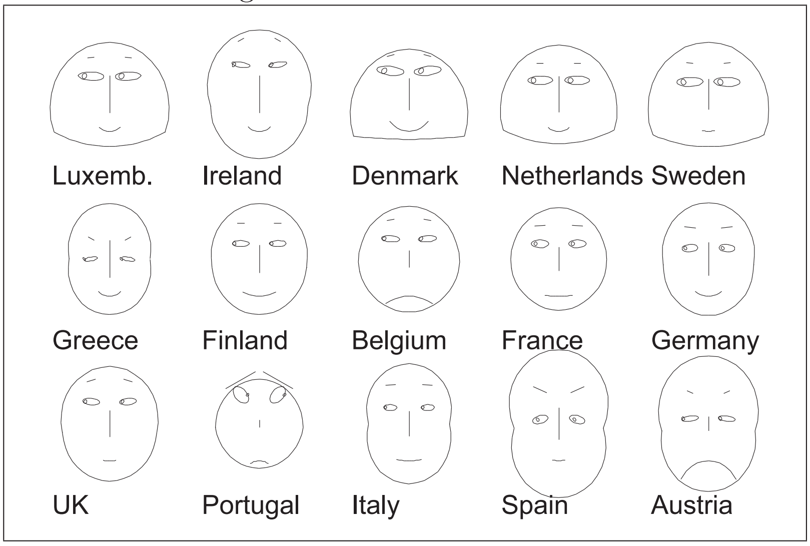
Chernoff's face comparison is executed with SURVO computing environment. (Mustonen, 1992, pg. 298–301). Chernoff's method of faces is based on 18 variables each influencing one aspect of the face figure. Variables not used in this comparison were eccentricity of upper and lower face, vertical position of mouth and separation

Figure 5.14: Chernoff's faces variables.

```
GPLOT NAAMA / TYPE=FACES
VARIABLES: xmin      xmax      Features                        fmin fmax
ODA_GNI    0.18444*  0.8867**  Radius_to_corner_of_face_OP      0.6  1.0
ODA_GNI    0.18444*  0.8867**  Angle_of_OP_to_horizontal        0.0  0.6
Aid_Var    22.9213*  75.177**  Vertical_size_of_face_OU         0.6  1.0
 -         *         **        Eccentricity_of_upper_face       0.5  1.5
 -         *         **        Eccentricity_of_lower_face       0.5  1.5
Loans_In   75.083**  0*        Length_of_nose                   0.1  0.5
 -         *         **        Vertical_position_of_mouth       0.2  0.8
Loans_In   75.083**  0*        Curvature_of_mouth_1/R          -4.0  4.0
Loan_Var   0*        218.92**  Width_of_mouth                   0.2  1.0
Aid_Inco   9.82794*  66.53**   Vertical_position_of_eyes        0.0  0.4
 -         *         **        Separation_of_eyes               0.3  0.8
Aid_Inco   9.82794*  66.53**   Slant_of_eyes                   -0.5  0.5
Loans_Ai   0*        103.78**  Eccentricity_of_eyes             0.3  1.0
ODA_GNI    0.18444*  0.8867**  Size_of_eyes                     0.1  0.2
Loans_Ai   0*        103.78**  Position_of_pupils              -0.1  0.1
Aid_Var    22.9213*  75.177**  Vertical_position_of_eyebrows    0.2  0.4
Aid_Inco   9.82794*  66.53**   Slant_of_eyebrows               -0.5  0.5
Loans_Ai   0*        103.78**  Size_of_eyebrows                 0.1  0.5
END
```

of mouth. Leaving out some variables is normal in Chernoff's face implementation process, as each data is different and includes different amount of variation. These variables were left out since they distorted the faces too much in this particular case. See figure 5.14.

Figure 5.15: Chernoff's faces.



Faces of each EU–15 Member State in figure 5.15 easily show the differences between the Member States. Countries with the highest scores, Luxembourg, Denmark, Netherlands, Sweden and Ireland appear to be more content than countries with low scores, such as Austria, Portugal or Spain. Although Greece places high in the comparison, it resembles visually Spain and other SD group Members. This is due to the fact that since Greece has not given any loans, it received high points in the index, but still was at the low end of other measurements concerning grants. Big–3 countries France, Germany and UK resemble each other quite well. Portugal and Spain both belong to the loan oriented end of the spectrum, but as is visually perceptible, they do in fact differ quite strongly in their grant – loan practices. The differences visually portrayed are to be analyzed with the original data presented in table 5.4.

The results of the Grant–Loan Index and its compliance with Carbone's model reveals interesting issues concerning the EU–15's debt practices. As Northern donors are mainly at the grant oriented end, Big–3 countries are both grant and loan oriented, and Southern donors mainly loan oriented, what does this entail of the overall picture? At least the differences in ODA volumes need to be taken into consideration when looking at this data; countries with large volumes have wider influence in terms of policies (official or unofficial) than the practices of countries with low volumes of grants, loans and debt relief. However, as some of the EU Member States have in fact a heavy focus on loan oriented ODA practices, the role of loans should be more visible in EU development policy framework as well. Next, the disparities within the debt policy are discussed by concluding the findings of debt practices and development policy framework in the final chapter of this study.

Chapter 6

What is the European Debt Policy?

In the quest of defining and analyzing the debt policy of the European Union and its Member States, vast differences between actors' individual policies have been determined both in long–term and short–term practices. This study has described (1) how the question of external debt of the developing nations appears in currently in force EU development policy framework's documents, (2) how EU–15 Member States have differed in giving grants, loans and debt relief to the developing nations by region and income since the 1960s to the 2000s and measured (3) the orientation of each EU–15 Member State in terms of grants and loans in ODA by developing the Grant – Loan Index. This study has been descriptive in nature and this study has used both qualitative and quantitative data.

The aim of this Master's Thesis has been to form a coherent perspective to what are the European Union's debt practices towards the developing nations' external debt. This issue has been approached from the perspective of development policy framework and debt practices while using an applied structure of policy analysis. Policy analysis was chosen as a method to complement the complex structure of these practices, of which no previous research from this perspective has been executed. Field of research linked to this issue was multiform as well, including political economy's perspectives to choosing either loans or grants as methods of development, the specific field of EU development policy, and the context in which interaction between the developing and the EU Member countries happens, i.e. the North – South conflict. History discussed concerned the origin and traditions of lending, as well as the meaning of past colonial relations in current policies.

The concrete approach of this study applied Carbone's (2007) study of different characteristics of the EU Member States' development policies in two ways. The groups used by Carbone were used in comparing grants (including debt relief as a separate item), and loans to different developing nations by five groups of region and income (sixth group in by region was unspecified and by income the unallocated groups, which both included same funds for development projects in donor countries, not the developing nations). Carbone's division was also used in the development of a Grant – Loan Index to measure the orientation of EU Member States' grant and loan practices. This comparison was aimed at forming a concrete way to specifically determine the differences between Member States in terms of the structure of ODA. As a result it was concluded that the Grant–Loan Index results are highly compatible with Carbone's findings, except in the case of Greece. However, the findings support the idea that structure of ODA links directly to its quality and more research should be put into the seemingly small, yet strategically important differences between the Member States.

The research question of this Master's Thesis was "What is the European Union's debt policy profile?". This question was approached from two different angles, which together form the debt policy; development policy framework and debt practices. Next, the key findings of each, the content of the development policy framework and debt practices, are summarized and compared in terms of the most relevant aspects in light of today's situation.

6.1 European Union's Debt Policy

The debt policy profile for the EU Member States is summarized in this chapter. First the content of development policy framework is discussed, followed up with a summary of the debt practices. They are compared, after which the challenges of the study and future study areas are discussed.

Development Policy Framework

The development policy framework included five different parts of the development policy in detail, the European Consensus on development, the Millennium Development Goals, Policy Coherence for Development, Intervention area of debt relief and geographical partnerships. The focus in this chapter was on how the issue of external debt appears in these documents / policy outlines of the EU development policy.

The Consensus called for further debt relief and finding solutions to the debt burden of the developing nations. Debt relief was seen as a method in reducing vulnerability to exogenous shocks. Countries which have experienced exogenous shocks and which are in post–conflict state, are mentioned of being in focus. Millennium Development Goals mentions the issue of external debt in goal 8, "Develop a global partnership for development". Sub–target 13 calls for addressing the need of the least developed countries, includes the HIPC and overall puts emphasis on rewarding those able and willing to fulfill the policy conditions set for debt relief. Sub–target 15 included dealing with the issue of external debt in a comprehensible matter in order to reach sustainability (of loan accumulation). Policy coherence did not mention the issue of financial practices with the developing nations, as expected, but in the discussion it was brought up that the approach could also be different and that it is important to note that it is not. Out of 9 different intervention areas of development, one, number 7, included debt relief within the support for economic and institutional reforms. In it the focus was on the HIPC and the MDRI. Since only 23 countries have completed the HIPC, it is possible to say that the HIPC Initiative is neither an easy nor necessarily the best global solution as discussed previously. More research is needed in this aspect as well. Finally, the geographical cooperation focused on the former colonies and the OCTs indirectly included the issue of external debt in the cases of Africa and the Pacific regions. In both of these cases the indirect reference was through the content included in the MDGs, which were included in the partnership.

Overall the existence of the issue of external debt in the framework of the development policy framework appears to be more narrow in focus (than needed), and not comprehensible. The MDGs was the only not entirely EU–focused component of the framework and it did include, if compared to others components, the only references to the need of having a "comprehensible approach" to the issue. In EU's own documents the references to the issue took often only one narrow perspective, such as the HIPC Initiative, and did not bring up analysis or references concerning the meaning of debt in the overall development equation.

Debt Practices

In the debt practices data loans, grants and debt relief to the developing nations were presented in different forms. It was concluded that new types of loans appeared in the OECD DAC statistics mainly during two time periods, 1960s and (mid–)1990s. It was also concluded that the Big–3 and the SD groups had the highest shares of sector VII "Action on Debt" and national comparisons revealed differences in variation. SD group had high variation of the sector, Big–3 group low variation. Sector VII activity was notably low during the 1980s for all donor groups. There were also some differences in timing of when sector VII was allocated high shares, for example Northern donors had significantly lower shares of the sector in the 2000s as opposed to the two other groups. Differences in previously given loan sums are perhaps the reason for differences in sector activities in recent years.

The differences in loans and aid within ODA for the three donor groups exist in terms of timing, stability and equality of the practices. Timing referred to differences in ("political") reaction times and chronological placement of practices or policy shifts, stability refers to (either high or low) variation in practices, i.e. changes in allocated sums or shares. Equality refers to how equal the groups have been in their practices towards different developing countries by regions and income.

More specific differences in debt practices data were found as follows. Loan sums; timing of lending, differing reactions to the debt crisis, and differences in relative impact of the actors's practices since volumes of loans differ substantially. Grant sums; differences in timing when grants were given, the stability of given sums, and similarities in grant sums within donor groups. Debt relief sums: differences in timing, stability and again, the volumes. Grants and loans by region: differences in (1) policies concerning Africa, (2) stability of loan shares, (3) stability of grant shares, and (4) growth of unspecified / unallocated sector. Debt relief: Africa has received the most debt relief over time, but Asia's share has grown in the recent years. Grants and loans by income concluded that (1) the LMIC group was the main recipient of loans for all groups, but differences appeared in (2) stability of given shares and (3) equality of practices. Debt relief: the LDC and LIC groups have received less debt relief than the LMIC group, which is most likely due to the fact that it has gotten the most loans as well. Highest income groups have received less debt relief than lower income groups, as expected and hoped.

In the comparison of ACPs versus non–ACPs it is found that ACPs have been favored in both debt relief and loans, but that grant sums have been more equal. ACPs received on average more debt relief than the non–ACPs and less loans on average than the non–ACPs when compared to group size. Since data is from 1988, and before current equalization of policies, results are expected. However, both average loan sums for the non–ACPs have been over 60% in the 2000s, and more debt relief has gone to the ACPs than the non–ACPs, except in 2007 and 2008, when opposite has occurred.

In the comparison between the EU DAC Member States and the multilateral organizations, it is found that volumes of grants have been similar; EU with annual totals a bit higher than the multilaterals. Loans have been also similar until the year 1992; multilaterals with a bit higher on average loan sums. Since 1992, EU Member States decreased loan sums significantly, which was a clear policy shift, as the multilaterals continued with increasing sums. Their financing does come partially from the European Union Member States and this interaction/cooperation should be further investigated. Debt relief sums are significantly different between EU Member States and the multilaterals; EU has given massive volumes throughout the time period in comparison to the MLs. Since in the current system some loans are channeled through the multilaterals but debt relief almost entirely given by the countries themselves, some indication of outsourcing politically "negative" actions to faceless multilaterals, while practicing positively toned actions in national level, does exist. More research into the relationship between the EU Member States and the multilateral loans is clearly needed.

Grant – Loan Index was formed to measure the orientation of the EU–15 Member States' grants and loans in ODA practices. This was done with six different variables based on ODA data available through OECD DAC. It was found that the NDs were grant oriented, Big–3 grant and loan oriented and SDs mainly loan oriented. One exception to the model was Greece, which placed in the midst of the Northern donors in the grant oriented end, although the country is a member of the Southern donors group. This exception was due to the Grant – Loan Index's emphasis on loans; if a country had not given loans, it would score high points. Model is concluded to be in compliance with Carbone's model concerning development assistance performance, with the exception of Greece, as mentioned.

Overall the Grant – Loan Index results reveal substantial differences in a short time period among the Member States' policies in all variables, especially the differences in Coefficient of Variation of grants and loans indicated that grant practices are in general more stable than loans practices, i.e. grants are given in a more stable and better thought–of manner. This is highly relevant when discussing the development policy practices overall. Further development of the Index could include more detailed comparison of those countries which have given loans in terms of bilateral relations, and for example the role of former colonies in each former metropolitan's practices. This study included all EU–15 countries and even those which have not given loans, since in this stage it was important to include all countries of the EU–15 to gain knowledge of the overall relationship between the donors. Different formulations of the Index could also be formed by including and excluding different (old or new) variables.

The EU-12 were not included in this study, but the relevance of their perspectives to the issue should not be excluded in future research. The fact that 12 of the current 27 EU Member States have not had debt practices, is significant. The large number of countries without debt practices will probably work as an obstacle to the possible forming of a separate debt policy or strategy. However, if and when these countries will become more active in debt practices and other ODA activities, the relevance and need for a comprehensible approach is again emphasized.

Table 6.1 presents the content of the "empty holes" in development policy presented in figure 1.1. Five most relevant differences in current development policy framework and past and current debt practices are included in this same table as a summary of those items most interesting and important in terms of studies in relevant fields as well.

The complexity of the issue itself is in a way mirrored in the results of both the development policy framework and the debt practices. The main argument of this study is, that the concrete debt practices of the EU-15 form a substantial part of overall development assistance. However significant in concrete actions, the role of external debt in current development policy framework is rather insignificant. Overall the disparity between the practices and development policy framework should be further investigated in relation to the concrete work in the EU towards reaching the goals set for the development policy, and in overall development of the development policy.

It is hard to estimate what kind of a world would exist if all unsustainable external debts of the developing nations were managed better or cancelled entirely, or if this had been done in the past. It might be that loan accumulation would start all over again, since loans do entail ceaseless opportunities. In the light of other discussed studies, this study and the found "existing contradictions" between the practices and policy framework, it is suffice to say that a more comprehensible approach in needed.

Table 6.1: Debt policy item comparison.

Development policy framework	Debt practices
Debt discussed within other items, not seen as one main issue in development.	Different kinds of loan types for a big portion of total ODA practices and the basic practices have existed since the 1960s.
Lack of comprehensible approach in EU documents (UN's MDGs only one demanding coherence).	Share of sector VII very high in total ODA for many Member States in the past and in current situation.
Focus on multilateral initiatives with policy conditions.	Variation high between practices of different Member States, yet similarities exist also within and between donor groups.
EU does not take or demand active role in the solving of the external debt problem of the developing nations.	Common features of actions between donors reveal that similar practices are conducted and a logical, although "unofficial", policy does exist. Carbone's group division applies well to the debt practices.
Based on the overall content, EU wishes to remain fairly distant from the problem by discussing it within and through other items, issue clearly left out of focus.	Overall practices concerning external debt management are numerous, and highly influential.

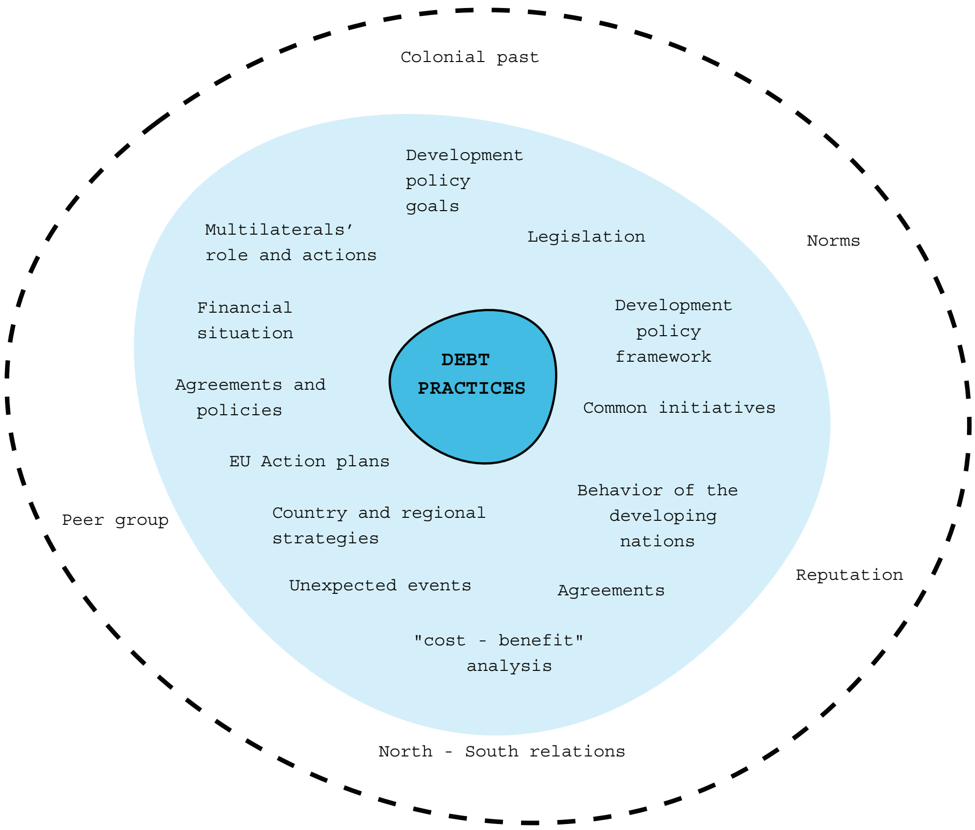
In addition to the debt policy item comparison, the structure of the main influencing factors relating to a country's debt practices are summarized here, see figure 6.1 for visualization.

The core factors influencing debt practices are presented closest to the center, and issues influencing both the practices, and the issues in the middle area, are listed in the outer sphere. Issues such as common initiatives, development policy framework, multilaterals, agreements and policies, actions plans, etc. are all influenced by the colonial period, and history, but also by "norms" (created by EU's own action) during the time period development cooperation has existed. The "peer group" is also listed in the outer layer. This refers to the wider influence countries appear to have on other EU-15 countries, this was seen for example in the debt practices data concerning sums where similar development have occurred[1].

[1]The more abstract concepts such as the peer group and norms have not been discussed in this study any further due to length limitations, and since the focus has been on allocated sums and policy content. They would however make a great future research area

What is evident form this study, is that external debt in global politics is an intriguing phenomena. It is not just a mere economic fact, but as Chomsky has stated, but a social and ideological construct (Global Issues, 2010). And as Eurodad concluded in 2010, there still is no comprehensible approach to the issue of external debt of the developing nations. This study has shown that in detail in the context of the EU.

Figure 6.1: Debt practices policy profile influencers.



Alternative Policy

As the differences between debt practices and development policy framework content have been discussed in detail, and the overall setup has been overviewed in other chapters of this study, it is order to discuss the alternative policy (or policies). This purely hypothetical analysis concerning the "what ifs" of the policy include two different "options" regarding the future of debt policy. In the current situation responsibility of the debt policy of each EU Member State has been left entirely in the hands of each member government. These governments have practiced widely differing policies. This fact or the other fact that development policy is a field of shared competence, should not limit the discourse or debate around debt policy or external debt management in the context of the EU. Alternatively, the EU could adopt a different approach to the issue in the future. On the basis of the findings in this study, there are two separate strategies the EU could adopt in the future.

First strategy option would be to improve the system step–by–step, without changing the already in–existence structures in the EU and shared competence in the field. This option could include firstly an outline for an official debt strategy. Debt strategy would include policy suggestions, which might be for example specific guidelines concerning lending and debt relief (to which income group countries and in which terms) and outlines concerning how large of a share debt practices could be in relation to given grants. Debt strategy would also need to alter the way the issue of external debt is currently represented in development policy framework and make it more visible, or vice versa explain why it is not emphasized. EU could also list all of its official debt practices, and define its official relationship with international lending organizations, including the Paris Club, IMF and World Bank. The role and significance of actors within the EU, such as EIB, ECOFIN, EDF should also be clarified. These actors are all interesting especially in terms of the internal policies they practice. The structure of OECD DAC statistics by type data could also be simplified to better accommodate researchers, and the number or geographical groups could be increased from five to about ten to give a better understanding of regional division of ODA.

Strategy option two would include practices that would require a massive re–organization of the current system. In option two most debt practices would be outsourced to a separate EU–level organization focused on the issue. This organization would be financed by all EU member governments. Member governments could participate in decision–making and in the outlining of a common internal policies. This organization could be placed under the European Central Bank ECB, which is in charge of the definition and implementation of monetary policy for the euro area; the conduct of foreign exchange operations; the holding and management of the official foreign reserves of the euro area countries and the promotion of the smooth operation of payment systems (ECB Tasks, 2010). This strategy would however require a massive change in the existing system but also in ideology, and its realization is of course improbable. Strategy one would be a plausible goal to reach at some point, but even that would require strong political will to push the issue on the agenda. Developing nations' external debt is not as "hot of a topic" as it has been before. Multiform good and functioning initiatives have been since started, which have improved the situation. The number or practices and initiatives has grown, and although the simple adding of practices does not solve the problem, the existence and emergence of several initiatives make the future of EU debt policy seem certainly more bright than its past since they do entail the assumption that the issue is important. Developments in the system during the past years have laid out a good starting point for a new and more comprehensible approach.

6.2 Limitations of Study and Future Research

This study has focused on the practices of the EU–15 Member States in the field of high external debt from the perspective of the relationship between grants, loans and debt relief in ODA. Due to limitations concerning length, this study has been solely focused on the actions of the EU–15 countries, not other institutions within the EU involved with loans and external debt of the developing nations. Data used has remained on a general level, and many details have not been included. The most relevant lack in analysis concerns the reasons behind policy choices of the EU–15 countries, which have been discussed here merely through theoretical analysis concerning plausible reasons behind selecting either loans or grants, or both. This subject would be more suitably studied as a content analysis concerning each EU–15 Member States' own policy outlines and the ways in which lending and debt relief has been motivated and justified, suffice to say based on this study, reasons for not giving loans are most likely different in the Northern than in the Southern donor groups, for example.

The field of external debt in the context of the EU is a highly interesting and fruitful field of research, where not much research has been conducted before. Findings indicate that more research should be directed especially towards the relationship between the EU Member States and the multilaterals, and all the actions of organizations within the EU involved with external debt, for example the European Investment Bank and the EDF. More detailed research into the policy choices of those countries which have not given loans at all, would also be interesting. Norms and peer groups influence on behavior of governments would also be a challenging research area. Newer Member States, the EU–12 were not included in this study, but their role in the development as well as debt practices should be analyzed in the future as soon as they activate in the field of development cooperation. Other applications of data in addition to the Grant–Loan Index are encouraged to better portray different aspects of the field.

6.3 Afterword

The completion of this study and the year 2010 approach their end at the same time. This past year has been an interesting year in both EU politics and especially concerning the question of debt. Debt has been in the headlines mainly in the context of national debt of the EU Members themselves, not the developing nations. Both Greece and Ireland have had to apply for loans from the global community in order to save their national economies from collapsing. It seems that in the EU we are still living in a state of balancing between crisis and catastrophe, which has lasted since the eruption of the financial crisis in late 2008. Looking back, it seems that loans have played a significant role in many crises, which remind us of the overall importance and difficulty of debt management. Although debt practices have been initiated since ”biblical times”, it seems that still the management of global credit is a challenge in many levels, in both the developing and the developed nations. Reasons and valid policy solutions for ways of managing global credit are truly needed, for which more research, to support policy choices and shifts, is the only viable solution.

The national debts of the EU Member States have directed the focus from the developing nations to themselves, but the Millennium Development Goals to be reached by the year 2015 have in fact evoked some activity in EU development policies in 2010 as well. The Millennium Summit held in September 2010 concluded, as explained, that the EU is lagging in its progress and a separate action plan with annual reporting has been set–up in late 2010. This again is one needed step towards developing the quality and impact of development assistance.

The results of this study should be utilized and used in the development of development policy and in analyzing the reasons why the EU is lagging behind in its progress towards the MDGs. What is the larger relevance of this study then? The overall approach and analysis method of this study could be applied in different fields of social sciences. The aim of this study has been to take a large entity with different components, and analyze them together in order to gain not previously known information. Social science and politics studies in all levels should not shy away from studying large and abstract entities due to the heightened level of difficulty often included, but to approach them with a combination of different data analysis methods and methodological tools. In the current era of globalization, the different bilateral, multilateral and private actors interact in a complex and vast web with its own rules and guidelines. Most interesting and currently relevant problems emerge from this complex cooperation and this is where most interesting research set–ups can be invented and applied in. This study is by no means an example of this, but is an example of a study where large entities are discussed in a hypothesis–generating spirit. This will hopefully inspire others in the future to develop this or similar data further and execute research with similar goals and set–up in mind.

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