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Article

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Intereconomics: Review of European economic policy

Provided in Cooperation with:
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Suggested Citation: Simonis, Udo E. (1977) : Some considerations on the external public debt of LDCs, Intereconomics: Review of European economic policy, ISSN 0020-5346, Springer, Berlin, Vol. 12, Iss. 7/8, pp. 204-207

This Version is available at:
http://hdl.handle.net/10419/122443

Some Considerations on the External Public Debt of LDCs

by Udo E. Simonis, Berlin *

The Federal Republic of Germany, together with the United States of America, is one of the most determined opponents to the developing countries' demand for a general debt moratorium (and also the UNCTAD integrated programme on commodities). However, the outcome of recent international conferences will not be without consequences for the actual relationship between Germany and the developing countries. At least the necessity of reconsidering possible arrangements has become clear, if a further isolation of the Federal Republic of Germany in the North-South dialogue is to be prevented.

One of the areas asking for reconsideration and needing new ideas is the mounting debt burden of most of the developing countries. It is even probable that here we find a crucial part of the North-South problems, inasmuch as the increasing amounts of loans and their hardening terms [1] have in many cases led to debt servicing problems of alarming magnitudes, what in turn threatens the smooth development of the international trade relations.

[1] On the Eurodollar market, in the second half of 1976, for the developing countries the interest added to LIBOR was 1.84 p.c. while that for the industrialized countries was 1.51 p.c.

Economic interdependence definitely has reached a point where the problems of one country or a group of countries have strong repercussions on the other countries. This became very clear after the so-called oil crisis as well as with the last economic recession. Besides of primarily economic interdependencies political interdependencies are strenghtening; interdependency is manifestating itself not only in the field of trade and direct investment but also in the growing political participation of the developing countries.

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Today, economic weakness is no longer identical with economic and political insignificance.

The Position of the Developing Countries

An UNCTAD report of 1976 and the World Bank's debt data for 1974 which have been published recently, give an impression of the order of the magnitude of the developing countries' debt burden. In the UNCTAD report the external public debt (defined as the debt incurred or guaranteed by governments) of 81 developing countries in 1972 is estimated at US $ 88 bn. This debt burden has a strong upward tendency: in 1961 it was in the order of US $ 21.6 bn (for 79 countries), then grew to $ 37.5 bn in 1965 and to $ 72.6 bn in 1972; debt outstanding at the end of 1974 reached $ 105.5 bn or $ 151.4 bn if indisbursed balances are included (figures for 86 developing countries). Furthermore, according to various estimations in 1977 the public debt burden of the developing countries has surpassed US $ 200 bn. This sum increases to more than $ 250 bn if the debts from private sources are added. Taking the Federal Republic of Germany out of the group of creditors shows that its credits to the developing countries alone amount to more than DM 80 bn.

The structure of the external public debt of the developing countries in 1974 by type of credit was as follows:

- Total official sources US $ 64.4 bn, of which $ 48.5 bn were loans from governments and $ 15.8 bn came from international organizations.
- Total private sources $ 41.4 bn, of which $ 28.6 bn came from financial institutions and $ 11.2 bn represented suppliers credits [2].

Nearly 10 p.c. of the total debt are due from those 15 developing countries which have an annual Gross National Product (GNP) of US $ 100 per capita or less, whilst their part in the GNP of all the 86 countries included in the survey is only about 4.2 p.c. About 64 p.c. of the total debt and 58 p.c. of the total GNP fall to 49 countries with a GNP of between US $ 100 to 500 per capita and year. The 17 relatively well-off developing countries with a GNP of more than US $ 500 per capita participate with only about 26 p.c. in the total debt burden but with 38 p.c. in the GNP of all the developing countries included. In other words: the amount (and structure) of debt differs according to the degree of poverty or wealth the country has attained. The poorer countries rely more on official, the better-off countries more on private debt.

Looking at the annual payments of the developing countries concerning interest and debt service also shows a tremendous increase, from only US $ 0.8 bn in 1956 to $ 13.5 bn in 1974, and approximately $ 16.0 bn this year. Since 1971 the debt has been growing at a rate of 20 p.c. per year, while the debt service payments have been growing at a much faster rate – more than 25 p.c. per year.

Over the past decades, the rate of growth of both debt outstanding and debt service payments has been twice the rate of growth of export earnings for the developing countries, and more than three times that of the GNP. The increasing amount of loans and their terms constitute, in many cases, an obstacle to economic growth and flexible management of the balance of payments. As R. C. Garg has shown in this journal ". . . it almost takes two dollars of fresh borrowings to materialize one dollar of net transfer of real resources" [3].

In a situation like this, the claims addressed to the industrialized countries on the international conference level will become more massive. On the other hand, most of the developing countries still believe that a positive economic development will be promoted in collaboration with the industrialized countries. Claims of this nature have been made and are to be expected for the forthcoming conferences, and they must lead to new areas of investigation.

General Possibilities of Dealing with the Debt Situation

The question of how to deal with the debt burden of developing countries has occupied some concern of different departments of the United Nations. In 1975 for instance, the Commission for Invisibles and Trade Financing nominated a group of government experts and gave them the mandate to study the factors influencing the national obligations concerning payment of interests and debt services. According to their proposals, no further negotiations concerning the debt of one country or the other should be held, but instead general considerations and measures should be convened allowing to keep these obligations within reasonable limits; legitime interests of the lending countries, on one hand, and the aims of development of the borrowing countries, on the other hand, ought to be safeguarded.

According to the predominant view of the developing countries, general directives should be established for interest and debt service payments and the related problems, and these directives should automatically be applied in every case of

[2] Data reported to the World Bank on the external public and publicly guaranteed debt with an original maturity of more than one year, as published in World Bank Debt Tables EC-167/76.

[3] Ramesh C. Garg, Debt Problems of Developing Countries, in: INTERECONOMICS, No. 3/4, 1977, p. 96.

borrowing. Specifically, developing countries have asked for: institutional arrangements to solve the debt problems; definition of criteria allowing to decide whether a country satisfies the conditions for mitigating the payment of debts; the elaboration of directives concerning the facilitation of payments, etc.

The industrialized countries, on the other hand – among them the Federal Republic of Germany –, are rather sceptic about multilateral agreements. They prefer to deal with the debt problems from case to case. The predominant opinion states that every country shows an individual structure of indebtedness and that the number of countries suffering heavily under their debt burden appears to be relatively small. Finally, it is often said that the capacity of making debts is an indicator for the economic capacity of a given country. Therefore it would be impossible to apply general criteria to judge the actual situation of the developing countries.

However, the propositions having been advanced, such as conversion and remission of debts, multinational debt settlements and debt moratoria do not give much thought to the question of how to remedy underlying basic structural problems. Even a remission of debts *per se* would not by itself change the structural problems of the developing countries. In fact, it would offer a chance for fresh borrowing but this might easily lead to the same situation as we have today. Therefore, the search for solutions should be more fundamental. New ways have to be taken and new solutions have to be looked for. However, these solutions should not be in total contradiction to the admitted principles of crediting and borrowing.

A New Proposition

After World War II the economy of the Western European countries was on a low level, foreign exchange and commercial relations were lacking. In this situation the European Recovery Program was of help. It provided industry and agriculture with the necessary means, allowing the reconstruction on the base of the know-how already present. It became possible, too, to give professional training to those who had not been working before or who had to be retrained. As far as possible we should draw from these historical experiences of the now highly developed countries.

In order to cope with the above mentioned factors, a new development fund is proposed here. This fund should actively contribute to reducing the economic problems of the developing countries by having an influence on the basic improvement of the economic situation, regionalizing development, providing resources for investment needs and shortage in foreign exchange, eliminating unemployment, training farmers and craftsmen, establishing efficient organizations (e.g. cooperatives à la Raiffeisen). These different and interrelated needs can only be tackled if there exist both education and capital. Regarding the latter the following principles for fund raising and crediting should be considered:

The capital of the fund proposed is raised partially or completely in that the creditor countries turn their official claims (credits by official sources) toward the developing countries – excluding the oil rich countries or concentrating on the least developed countries in particular – into investments in the fund to be established. Interests and debt service payments by the developing countries do no longer flow to the creditor countries but are turned to the fund. In this way, the fund is fastly growing and acquiring, in the course of time, considerable assets, as can be expected from the figures quoted above.

Regarding credit giving by the fund the following should be said generally. From the accumulating payments of interests and debt services the fund gives new credits to debitors in the developing countries, whereby the governments of these countries should only be one debitor among others. For these crediting activities guiding principles orientated towards development policy are to be established and followed, especially with respect to either promoting export performance or reducing import dependence of the developing countries.

What does this proposal contain? It should be stated clearly that this proposition does not mean the total remittal of the actual debts of the developing countries but instead means a slow, continuous transfer of the creditor countries' claims into an international fund. The basic economic principle that borrowed money must be payed back, therefore, is not violated. The repayment of former bilateral public credits and the new credit giving means above all an enlargement of the multilateral organization of credits. However, given certain conditions, the new fund could also play a clearing function for regional trade, thus stimulating the rather weak trade relations between the developing countries. (The importance of clearing especially for countries with small foreign exchange reserves has been demonstrated by the foundation of the European Payments Union [EPU] which had become possible and necessary by the Marshall Plan.)

It is not necessary here (and not interesting) to discuss in detail how the administration of the fund could be organized, how it could guide its activities along decentralized lines, whether or not it should be attached to one of the existing international institutions. This should be done separately and therefore needs not to be examplified here.

Important is that the idea gets off the ground that the payments of interests and amortization by the developing countries need to be re-channelled into new development activities in the developing countries, instead of transferring them back into the general government budget of the donor countries. Furthermore, although a high moral discipline seems to be needed to implement such a fund, safeguards must be provided to prevent it from becoming a new neo-colonial institution by touching too severely the autonomy of the developing countries. At the same time, of course, it must be avoided that such a fund becomes a "weak point" by asking too much from the developing countries' side. Finally, it should be added, that given sound principles, aims and the necessary institutional arrangements, the new fund could of course practically start with just one creditor and one debitor country, or with a group of countries, respectively.