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Countries' Repayment Performance Vis-à-Vis the IMF

A Response to Bäcker

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Mr. Bäcker makes the valuable point that the role of political and sociopolitical factors in countries' debt servicing performance needs to be considered. The IMF Working Paper version of our IMF *Staff Papers* article (Aylward and Thorne, 1998) dealt with the political environment, via three approaches. These included (1) comparing the incidence of adverse or irregular political events (i.e., frequent or sudden changes of government, civil war, or civil unrest) in the countries making late repayments to the IMF versus those making timely repayments; (2) contrasting the two groups according to a country political risk indicator published by a private country risk analysis firm; and (3) searching for temporal links between a country's political circumstances and the interruption of timely repayments to the IMF. While the latter approach was the most subjective, requiring a case study approach, its results nonetheless are worth noting. In about half of the 30 incidences of protracted arrears to the IMF that were analyzed, political events that may have influenced a country's external debt repayment performance could be temporally linked to the emergence of repayment problems vis-à-vis the IMF. But such an association could not be established in numerous other country cases for the reason that strongly unfavorable political conditions had persisted for many years before the emergence of arrears. In other cases, countries exhibited a continuously high level of political instability over a long period but incurred IMF arrears only intermittently, and then for a relatively moderate duration. Moreover, some of these countries went on to become and remain current with the IMF even while the same difficult conditions (e.g., a civil war) persisted. Thus, it is difficult to identify "turning points" when it could be judged that the cumulative impact of political difficulties either became bad enough to contribute significantly to the interruption of payments to the IMF, or improved sufficiently to explain an exit from arrears. Casting a wider net than just repayment performance vis-à-vis the IMF, Rivoli and Brewer (1997) found that for 199 rescheduling events over the period 1980–90, armed conflict was a significant predictor of debt servicing difficulties, while indicators of governmental regime change and of governmental legitimacy consistently lacked predictive power.

It is worth noting that the types of political circumstances considered in Aywlard and Thorne (1998) and Rivoli and Brewer (1977) are quite different from those that interest Mr. Bäcker (1998). Since his basic approach is that government chooses a debt-service level that maximizes the support for its policy among a population composed of distinct groups of citizens who assess differently the costs and benefits of sovereign debt repayment, the recent work of Bussière and Mulder (1999) may be more relevant. In testing for the influence of political instability on economic vulnerability specifically in the context of the 1994 and 1997 economic crisis episodes, these authors construct variables for political polarization, the political cohesion of the government, electoral indecision, and the impact of the timing of elections. They find that political instability has a strong impact on economic vulnerability in countries with weak economic fundamentals, while countries with a sound economic environment are only marginally affected by political instability as measured by these variables.

A quick conclusion based on these studies is that while politics clearly matters for countries' economic performance, how, why, and when it matters is not easy to explain. Much interesting work remains to be done in modeling how political factors impact debt servicing, growth rates, susceptibility to currency crises, and other facets of economic performance.

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