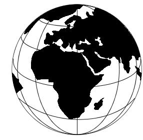
Geo Factsheet



Number 78

Third World Debt - Recent events

In September 1999, the World Bank in Washington DC agreed to help 19 of the world's poorest countries by writing off huge amounts of their debt. The first countries to benefit from the Heavily Indebted Poor Countries (HIPCs) initiative would be Nicaragua, Tanzania and Mauritania.

The HIPC initiative was launched in 1996 by the **World Bank (WB)** and **International Monetary Foundation (IMF)**. 41 of the world's poorest countries were singled out to get debt relief. To qualify, countries had to:

1. Prove that their debt was unsustainable, i.e. that it would be impossible – not just difficult – to pay it off. In practice, this meant having export earnings and GDP which were a fraction of their debt. It was argued that cancelling this debt would actually cost nothing because it could never be repayed anyway;
2. Agree to IMF economic policy for three years. After the three years, the countries were then said to have reached **decision point** when a debt relief package would be agreed;
3. Agree to follow IMF economic policy for another three years, following which debts would be written off.

The Jubilee 2000 campaign had pressurised western governments to accept a one-off cancellation of the unpayable debts of the world's poorest countries. A coalition of 70 organisations in 40 countries supported the campaign. The major aim of the initiative was to reduce the debt burden of poor countries to "sustainable" levels – i.e. to a value about 200% greater than their annual earnings from exports.

One of the conditions of the debt relief is that countries only continue to get help if they agree to follow IMF approved economic policies. This includes channelling any money saved into **anti-poverty** measures, especially basic services. The IMF lends countries money on condition they implement economic reforms known as **Structural Adjustment Programmes** (SAPS). SAPs usually mean cutting public spending and can have far-reaching harmful effects (Fig 1).

Key Terms

Commercial debt:	Poor countries owe banks money
Bilateral debt:	Poor countries owe another government money
Multilateral debt :	Poor countries owe the WB/IMF, who have drawn together money from several countries Most third world debt is multilateral.
HIPCs:	Highly indebted poor countries
World Bank:	Provides money for development programmes
IMF:	Lends money to countries with short-term cash-flow problems

Cancelling the debt

The IMF have put forward $3bn by revaluing their gold stocks, the UK put forward $221m, the European Development Fund put forward $700m, the US put forward $600m. Total debt relief came to $50bn.

The new changes to HIPC have gone through three stages:

1. The IMF had to be persuaded that HIPC was not working. This proved difficult, but the Jubilee 2000 campaign raised public involvement and led to demonstrations in many countries, including the G7 heads of government summit in Britain in 1998 and in Cologne in 1999.
2. Raising the money to increase debt relief, to get 26 countries into HIPC by December 2001. 14m ounces of IMF gold was revalued – its value was increased and this provided $3bn. The World Bank raised $2.5bn.
3. Rich countries were persuaded to make bilateral contributions to the HIPC trust fund. By the end of September 1999 this totalled $570m, but pressure from Britain has secured a commitment from European countries and the US so that this will increase to $1500m.

The challenge is to ensure that debt relief is effectively linked to poverty alleviation, especially health and education. However, critics point out that this still only goes one-third of the way to hitting the UN target of halving global poverty by 2015. It is also felt that six years is too long for poor countries to stick to rigid IMF policy.

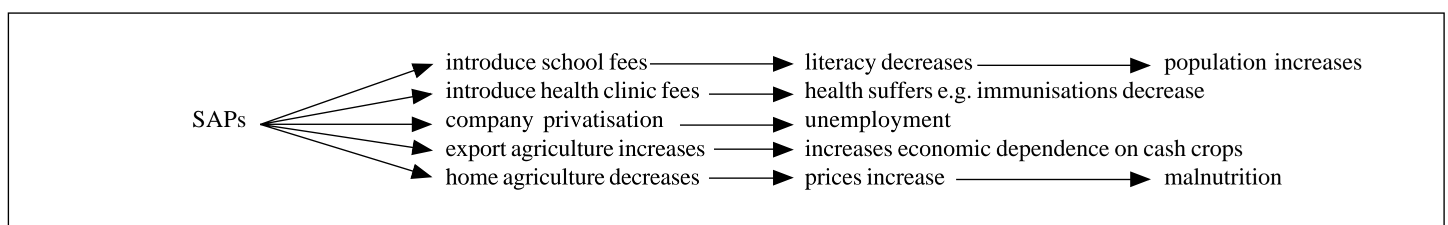
Origins of Debt

Commodity prices fell sharply in the 1970s and exports crashed. Third world countries borrowed money from western banks and the World Bank at very low interest rates to finance investment and to compensate for low export earnings. During the 1980s recession, western banks increased interest rates. At the same time, third world countries were earning little from their exports.

Soon the repayments were huge in relation to the original amount borrowed and countries were unable to repay the interest. 41 countries are classified as HIPCs and owe $1215bn.

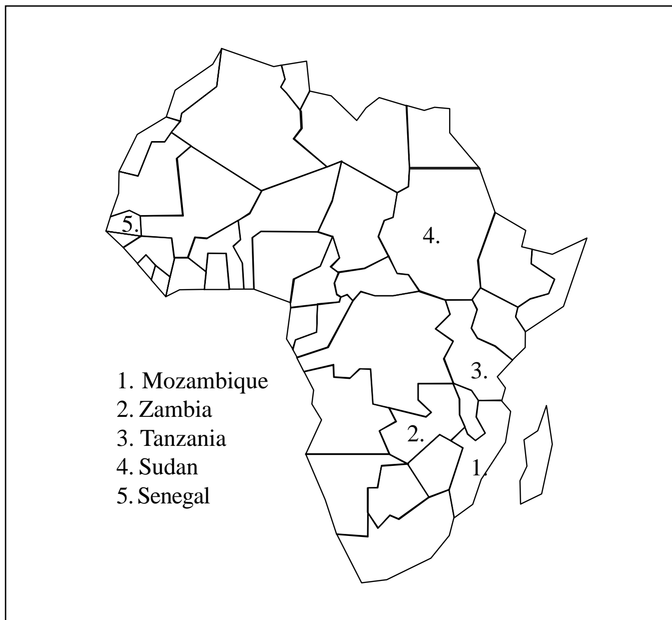
Newly independent African countries borrowed very heavily from the World Bank, the USA and the African Development Bank, but such countries were led by inexperienced governments. Projects were often poorly designed and infrastructure projects failed. Huge sums were spent on factories and other forms of industrial development which never became productive, i.e. never yielded any economic return.

Fig 1. Consequences of Structural Adjustment Programmes (SAPs)



In 63 of the 69 countries where the World Bank imposed SAPs, external debt actually increased over the period of the programme. The World Bank acknowledges that countries in Africa which followed IMF SAPs had slower growth in agricultural production than countries which were not following the structural adjustments.

Case Study: Africa



Case Study: Sub-Saharan Africa

Sub-Saharan Africa, excluding South Africa, has debts of $230bn. Debt-service payments (repayments) amount to $12bn annually – about four times what the region spends on health and education. Per capita debt is £365 but GNP per capita is only $308. Population is rapidly increasing (Fig 2)

Fig 2. % of global population living in SSA

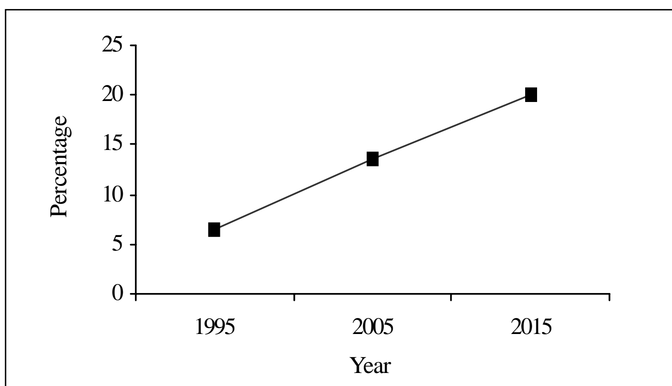
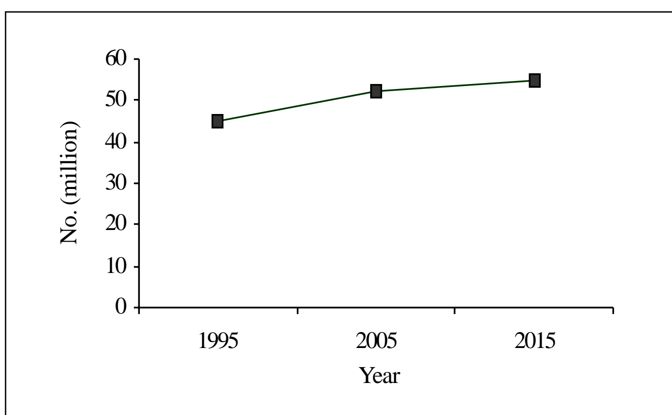


Fig 3. No. of children not receiving education



The region has obtained some debt relief in the form of debt-for-nature and debt-for-development swaps. In these, a Non-Governmental Organisation (NGO) takes over some or all of a country's debt from the bank at a substantial discount. The NGO then restructures the debt by passing along some of the discount given by the bank. The NGO accepts repayments in local currency, but then uses these repayments to finance local projects – national parks, health centres, etc. In this way, Madagascar has cut its $100m commercial bank debt by 50%.

However, many people have argued that too many countries in the region are excluded from HIPC status.

33 of the region's 44 countries are classified as HIPC by the World Bank. Ironically, the poorest people of these countries seem to have benefited little from the loans. As a condition of the loan, the IMF SAPs force the government of the country to cut public expenditure. SAPs have been repeatedly imposed on almost every country in the region since 1981.

SAPs have resulted in:

1. *Currency devaluation*
2. *Decreased spending on health - 40% of the region's population suffer from malnutrition*
3. *Increased taxes and interest rates*
4. *Increased unemployment*

Infant mortality has increased in the region as has unemployment. In the 1980s average real wages decreased in 26 of the region's countries.

Case Study: Sudan

Sudan has recently started paying the IMF $3.3m per month in order to settle its $1.5-1.7bn arrears. For the last 16 years, the IMF has suspended credit facilities to Sudan because of the country's inability to repay loans and because of the failure to implement economic reform.

Case Study: Senegal

- *IMF SAPs began in 1986*
- *SAPs resulted in:*

1. *Devaluation of currency – this doubled the cost of imports such as medicines. Maternal mortality increased between 1987 and 1991.*
2. *Abolition of government agricultural supply projects.*
3. *Domestic food production, e.g. vegetables, millet and corn decreased whilst export food production, e.g. of groundnuts, increased. In 1996, an estimated 22% of children were suffering from malnutrition.*
4. *Education expenditure decreased, but 67% of the adult population were illiterate.*
5. *Health care expenditure decreased – limited by the IMF to 3% of GDP, even though the World Health Organisation (WHO) recommend a 9% minimum.*
6. *Unemployment in Dakar increased from 25% (1991) to 44% (1996) and 10% of Senegalese children are estimated to be in employment.*

Case Study : Africa (continued)

Case Study: Mozambique

Mozambique joined the World Bank and IMF in 1984. SAPs were imposed in 1987 and toughened measures imposed in 1990. By 1990, Mozambique had become the most aid-dependent country in the world, with 90% of foreign aid dependent upon IMF/World Bank regulations.

The IMF saw inflation control as a priority, and this meant government spending was extremely tightly controlled. Unfortunately, this did not take into account the war which had devastated the country. Without spending it was simply impossible to increase industrial production.

*In 1996, the cost of servicing the debt, i.e. repaying the interest and the principal sum was twice the amount spent on health and education. But 24% of children born die before the age of 5 due to infectious diseases. Recently, the **Club of Paris**, the group of major lending (i.e. creditor) nations, agreed to reduce Mozambique's total debt by 80% ($2bn), later by 86%. But Mozambique immediately argued that this was insufficient. Mozambique was left owing Russia $509m (for military equipment) to be paid over 33 years at an interest rate of 0.8% per annum – an unsustainable debt. It is also worth noting that countries such as Nicaragua, Guinea Bisau and Tanzania also have huge debts to Russia.*

Problems of dealing with this Russian debt meant that Mozambique could not enter the HIPC classification. Mozambique needs $1.56m to decrease its debt to "sustainable" levels – much more than any other country.

Case Study: Zambia

Agriculture

- *IMF imposed SAPs prevented farmers obtaining credit for production and marketing of their goods.*
- *State marketing agencies for agricultural production were replaced by private agencies and the prices which farmers received for crops such as maize fell.*
- *Bartering of maize for commodities such as soap increased.*

Education

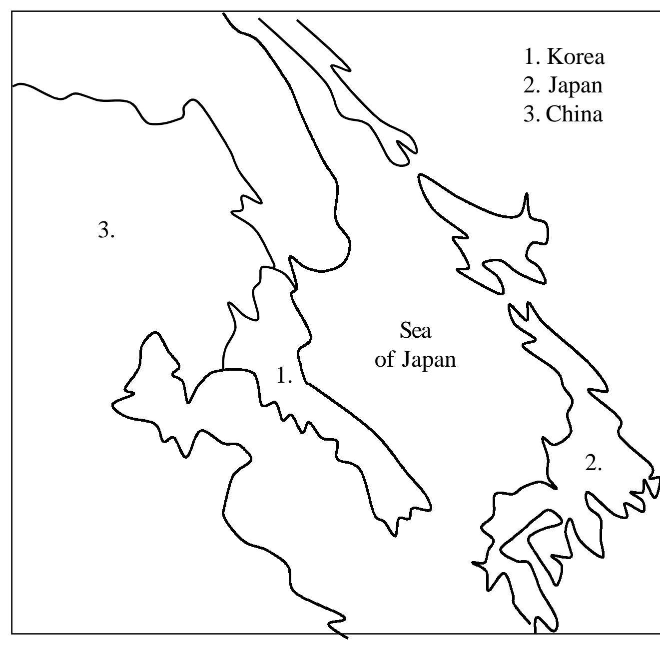
- *The national education budget decreased by 7% between 1985 and 1997.*

Health

- *Registration fees were imposed at health centres*
- *Immunisations decreased for measles and whooping cough.*
- *Infant malnutrition increased*

Case Study: Korea

- *At the start of 1999, South Korea was the world's eleventh largest economy.*
- *By mid-99 it emerged that the country's foreign debt was $200bn*
- *South Korea's debts emerged in a haphazard fashion – the government was very slow to disclose its true level of debt and this has meant that many lenders have lost confidence in South Korea.*
- *IMF have decided that South Korea adhere to international standards for bookkeeping!*



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