

International indebtedness of developing countries

Mezinárodní zadlužení rozvojových zemí

VLADIMÍR JENÍČEK

*Faculty of International Relations, University of Economics, Prague,
Czech Republic*

Abstract: The problem of international debts is, by its character, one of the most complex problems which the world economy is now facing. It complicates both the global balance of payments and the financial – credit system stability, with pronounced negative impacts on the currency stabilisation. It hinders the development of international economic co-operation and its higher forms – international economic integration. It is one of the reasons that the symmetrical forms of interdependence are pushed off and displaced by the asymmetrical ones. The global debts problem deteriorates, namely during the last time in interaction with the negative manifestations of the global problems (for example, at present very strongly with the environmental problems), the complex international co-operation climate.

Key words: debts, developing countries, payment ability, debt indicators

Abstrakt: Problém mezinárodní zadluženosti je svým charakterem jedním z nejkompexnějších, jakým nyní čelí světová ekonomika. Komplikuje globální platební rovnováhu a stabilitu finančního systému s výraznými negativními vlivy na měnovou stabilitu. Brání rovněž rozvoji mezinárodní ekonomické kooperace, včetně mezinárodní ekonomické integrace. Je to jeden z důvodů, proč symetrické formy vzájemné závislosti jsou nahrazovány asymetrickými. Problém globální zadluženosti zhoršuje, zejména v poslední době, ve vzájemném působení s dalšími negativními projevy klima mezinárodní spolupráce a stabilitu světové ekonomiky.

Klíčová slova: zadlužení, rozvojové země, platební schopnost, dluhové indikátory

The present form of international debtness was created gradually from the rather marginal malfunctions of the international economic relationships system between the wars and in the immediate after-the-war period. The stabilisation period, which in the world economy lasted for the whole 50s and 60s, created the atmosphere of carelessness, supported by the sufficiency of free business as well as credit capital. The extending capital market covered without many problems the needs of developing countries. At the beginning, it regarded namely governmental or government-guaranteed loans and credits, which were, however, very often used inefficiently, for consumption and unnecessary aims, prestigious projects, administration, army and for covering the payment balances deficits. Only rarely were they utilised for modernisation and restructuring of the developing economies, since a considerable part of them was not limited to the given purpose. The “cold war” atmosphere and the confrontation of the two world

systems rather supported this atmosphere of the foreign resources non-rational utilisation.

An especially important change occurred at the beginning of the 70s with the emerging structural crises, the so-called primary products price revolution, and with the successful OPEC activity which led to the first oil shock. There was enormously accelerated the developing countries differentiation, when some of them increased their economic level rapidly through the tenfold oil prices growth. With the majority of them, this collided, however, with the inability to absorb the so-called petro-dollars surpluses in their own economies, so that, at the beginning, most of them was thesaurised in the OECD countries banks. Only a minority of them went before the end of the decade through the so-called process of the re-circulation and loans to the less happy developing countries, namely the Moslim ones.

A great paradox of this period was that the enormous additional funds had considerably worsened the

Supported by the Ministry of Education, Youth and Sports of the Czech Republic (Project No. MSM 6138439909).

foreign debt problems just in the 70s. Not only did the sum of debts increased five times, but the problem changed also in quality, it grew over from the so-called sub-global to the global stage. The reason of this was the euphoria wave surging up in the enriching DCs, unreasoned expectations of great private banks with the issuing magnanimity in supplying new loans and credits and also the neglected activation of the regulation and corrective mechanisms which, unlike the energetic problem, were lagging behind considerably in the credit-financial sphere (Berger 2003).

Great private banks credits prevailed and replaced the governmental credit and loans, unfortunately very often without the necessary guaranties, however. All these mistaken expectations and decisions regarded all segments of the world economy – developing countries, the developed market economies as well as the centrally planned economies.

Their negative impact worsened still more at the beginning of the 80s with the fall of the primary products conjuncture and the second oil shock. Already in 1982, there became obvious the signals of the open debt crisis outbreak, which really bore out fully in the following year. The catastrophic scenario of the international financial-credit system breakdown shifted from the hypothetical danger to the stage of a real threat, supported by the avanturist attitude of some DCs leaders.

HISTORY OF DEBTS

Fortunately, these attitudes did not find support even in the majority of the DCs, and also the international financial organisations, together with some specialised U.N. agencies, found enough strength to accelerate the regulation measures. The debt crisis passed into a phase still dangerous but not threatening with fatal consequences any more. The pressing character of the debt problem also modified the increased volume of foreign direct investments considerably.

In 1987, the sum of debts overreached the “magic limit” of USD 1000 bill, but at the same time, the impact of the series of bilateral a namely multilateral measures started to show their results. During the last decade, the indebtedness still grew from USD 1000 bill. Up to approximately USD 2500 bill (at the end of the 90s), but its growth rate has rather slowed down in the DCs, but, on contrary, it increased in the former CMEA countries. On the other hand, the foreign debt problem has rather complicated by the consequences of the “real socialism” collapse, dissolving of the CMEA, the breakdown of the U.S.S.R. and a heavy economic drop down in most of the transforming economies. Another

negative symptom of the debt crisis is its pervading into other problem areas of the global character, such as the environmental ones. To a certain extent, the creditors still remain the “hostages of the debtors”.

Based on the recapitulation of the foreign debt problematic genesis, it can be concluded that there exists a continual tendency of its qualitative characteristics strengthening. Its causality is of the subjective as well as objective character and it was worsening for years by underestimating its scope and implications, what issued into the present situation, which is as follows: a total majority of the theoretical as well as economic-political analyses tend for years already to the opinion that the situation cannot be solved by the traditional methods and that it is equally impossible to sustain, at least in its main features, the postulate of the non-acceptance of the debt relief for the most heavily indebted countries. It is already realistically admitted, that most of these countries cannot ever repay their debts and that even the simple debt service (interest and pay-back) is already getting out of control and calls necessarily for new loans, with the preference of short term measures with often environmentally or otherwise negative effects. This has a disastrous impact on the international economic co-operation in many of the vitally important areas. It is enough to realise that only the debt service in absolute numbers amounts at present to over USD 3000 bill per year, the main part of which the DCs and TEs have to borrow again. It is thus the “vicious circle”.

It damages namely the sphere of international trade with goods and services, where the delinquent interests and the insufficient bonity of the debtors complicate the development of this sphere of economic relationships considerably. The most heavily indebted area – Latin America – is considerably hindered by the debt crisis in its integration endeavours as well as in the co-operation with its North American partners. This showed in a marked way for Brazil in the year 1999/2000 and in a quite disastrous way for Argentina in February and Uruguay in summer of 2002.

Finally, the last negative feature of the present period is the further technological lagging behind of the developing world, when the lack of foreign currency hinders the import of equipment as well as of the know-how and leads in its consequences to pushing these countries to the periphery of the international division of labour (Tichá 2008).

The main structural characteristics and their trends (see table) testify to the fact that namely the poorer and heavily indebted countries have at present only a very small chance to get any further credit capital (of course except the concessive help of the ODA, IFAD and other types).

Paradoxically, foreign indebtedness grows at present in the most accelerated way in the more developed DCs including the newly industrialised ones, in which the growing export ability ensures, however, the bearable level of the creditor risk, but it brings even here also a great dangers, as it was shown by the so-called “Asian shock” at the end of 1997, as well as all three Latin American shocks (1994, 1999 and 2002) (Williams and Nguyen 2005).

PAYMENT ABILITY

Payment ability of the heavily indebted countries – and that both the least and middle developed ones – is developing in a very unfavourable way. There has not occurred any decisive change in the payment ability trend, since the tendencies of the foreign trade development have not changed in any decisive way and the debt service has then been slightly relieved for the poorest countries, but not to such an extent that it would have abolished the basic trend. In average, payment ability has further worsened for the whole developing world.

At present, the debt service approaches approximately one quarter of the total sum of the DCs exports. Net outflow of the financial means from the DCs (the sum of credit instalments and interests) overreaches the inflow of resources already since 1987. This is very illustrative regarding the interdependence of the world economy and its other segments (Amel et al. 2004).

From the Table 1, it follows that private credits (namely those from great commercial banks), which were the main driving force in the second phase of the debt problem increase, are, after the sobering experience of the 80s, roughly equivalent to the official resources (of governments and international organisations except the IMF). Only in 1996 the internal revitalisation showed off. Namely the long term indebtedness increases continually, while the short-term one creates only a less important segment of

the total global indebtedness. The mentioned inability to pay debts is testified for by the development trends of the indebted group together with the debt burden distribution, the centre of which lays just in the poorest countries and regions of the world. The precise structural frame of the debt burden is now difficult to follow since in the second half of the 90s, the World Bank stopped publishing the yearly World Debt Tables and the data in the Global Development Finance (published once in two years) is structured in a slightly different way. Therefore, it is impossible to reconstruct the trend of the rate between the official and private resources (see above); however, the main tendencies are still obvious (the growth of the total foreign debt, the rate of the long-term and short-term indebtedness, the share of the IMF).

The debt service indicators (Table 2) are now followed according to the newly defined groups (including TEs). In this contribution, we will still observe the traditional structure of the World debt tables. According to that, we get the following data and development trends:

From the structural aspects, it is necessary to consider that the private bank debts (long-term and short-term) are still keeping the leading position, but they are not growing considerably any more. The multilateral and bilateral debts have begun to grow slightly again in the consequence of the international financial organisations activities in the frame of the initiatives and the insurance and correction mechanisms connected to the adaptation process.

An interesting phenomenon, which modifies the global indebtedness problem to a considerable extent at present, according both to its structure and importance, is a great increase of the direct foreign investments into the DCs, the share of which in the capital flows into the DCs has increased more than two and a half times only in the period 1990–1993. Some experts argue that this development mitigated the pressing character of the problem since it was one of the main factors of the less steep growth of the debt curve.

Table 1. Development of the DCs foreign indebtedness, 1970–2000 (mill USD)

Foreign debt category	1970	1980	1990	2000
Total debt of all DCs including TE	–	603.3	1 443.9	2 465.1
Long-term debts	44	377	1 107.8	1 728.5
– from official sources	31.7	170.5	595.2	819.9
– from private sources	12.3	206.6	502.6	608.9
Short-term debts	–	146.5	241.4	381.4
IMF sources utilisation	0.8	11.6	34.7	61.5

Source: The World Bank (2008)

Table 2. Structure and indicators of the debt group in the selected years of the period 1987–1994

Groups of countries and regions	Share in the total world indebtment in 1993	Rate of debts to export (%)			Rate of debt service to export (%)		
		1987	1993	1994	1987	1993	1994
Developing countries total	100	194	172	167	24	18	17
– heavily indebted	36	395	410	364	30	25	22
In that with low income	11	522	552	593	26	18	19
In that with middle income	25	363	368	310	31	27	23
– lightly indebted	43	221	212	209	28	27	26
Sub-Saharan Africa*	12	253	254	255	19	15	12
East Asia and Pacific	20	131	101	100	25	14	13
Europe and Middle Asia	20	115	164	168	19	15	15
Latin America	29	378	261	247	37	29	29
Middle East and North America	11	163	153	153	16	17	16
South Asia	8	294	289	249	28	25	23

Note: *Including South Africa Union

Source: World Bank, Debtor Reporting System, according to World Debt Tables 1994–1995, Vol. I, p. 27

However, others argue, that this investment capital has flown purposefully into only few countries (cca 15–20 DCs and China) and left the other completely outside the sphere of interest, and that it has probably decreased the sum of the disponible loan capital, so that globally it rather complicated the indebtment problem still more. Anyway, this phenomenon is worth mentioning and it can be evaluated as a specific form of the adaptation process, however, obviously with both positive and negative aspects. After the stabilisation of the FDI flows in the years 1994–1997, a strong inflow of the FDI portfolio capital was expected also into the Asian countries which most suffered from the “Asian shock”. However, the situation was complicated by the Latin America financial disturbances of the years 2000–2002, which exhausted many national and international investors and donors.

The whole adaptation process started later than those regarding the other core problems (for example energy) but the adaptation accelerated conspicuously in the second half of the 80s, and that namely in two basic directions.

- (a) official initiatives of the multilateral character
- (b) in the conversion and capitalisation operations and techniques of the foreign liabilities secondary market.

Regarding the official initiatives, their beginning can be placed into the mid 80s, when there won the notion that the core of the debt crisis does not lay in the temporary insolvency of some countries, but that it is a global and a very complex problem, in which the whole system of credit, wage and capital relationships

has to be engaged through the international financial organisations and the governments of the main creditor countries. The initiatives gradually presented at the international forums thus usually bear the names of these organisations or governments (Baker’s, Bradley’s, Brady’s, Connabler’s, Robinson’s etc. plans).

The Baker’s and Bradley’s plans were presented at the beginning of this new etap. Their merit laid in supplying new loans, eventually restructuralisation or debt relief for the countries agreeing to the market-oriented economic reforms. They did not come through because they did not bring completely new forms of the debt regulation, only a certain kind of the modified traditional restructuralisation approaches.

Only the Brady’s plan and the activities of the Paris Club and later on the London Club of the creditors consortium accepted fully the principle of the debt burden restriction and, at the same time, tried to utilise the foreign indebtness problem also from a certain more complex positive aspects, that is as a latent tool to solving also other (for example environmental) problems of the DCs. Two subsequent activities of the Paris Club diminished the sum of debts in some of the most heavily indebted DCs (Egypt, Argentina), but also the former CMEA countries (Poland). The importance of these official initiatives lies in replacing the sharply confronting attitudes by the principle of looking for compromises and solutions acceptable for both sides. However, their final result should not be overestimated; it could meet with success and be further developed only under the condition of amendments of the international financial relationships as a whole.

The source of pessimism lies just there. The foreign indebtedness problem is so complicated at present, that not only its solution, but even its regulation calls, on one hand, for the complex solution methodology at the scientific as well as economic level, on the other hand, it requires also co-ordinated activities and political will of all the subjects included. Both are still missing; outwardly it is manifested by the prevailing sterile rhetoric on the world top negotiation fora and the impossibility of reaching consensus in the strategic questions.

The situation is still worsened by the payment ability collapse in almost all the former CMEA countries including the successor states of the U.S.S.R. On the other hand, these countries are in strong need of the foreign capital inflow, both credit and business investments. For example, the financial situation of Russia is completely catastrophic at the beginning of the new millennium.

Thus, these countries will unavoidably get into confrontation situations with the DCs. The former creditor world area – the Eastern block – not only disappears from the world map, but it becomes a competitor of the developing world on the macro level of the individual investment activities. This will unavoidably strongly deteriorate the development forecast and the debt crisis solution for the whole beginning of 21st century (Table 3).

This forecast is negatively conditioned also by other conditions. The total world economy climate is not very positive for solving of this problematic since there is sustained a rather non-stable phase of the world market economy development for several years already, and only very few countries have been spared of it. Only after 1994, a certain revitalisation has manifested in some of the DMEs (i.e. USA, Great Britain, Canada), which was only partially and with a delay transferred into other countries. At the beginning of the 21st century, both the “American” as well as the “European” centre show only a slight growth rate and, moreover, the EU fights the financial budget problems.

One of the main consequences is the “drying up” of the capital markets and the lack of the free speculation credit and business capital. The traditional comparative advantages are gradually either modified or totally eliminated by the accelerated scientific and technological progress. In this situation, a fierce competition is growing in these markets. The whole atmosphere will not be very favourable to the “official initiatives” so that the debt regulation problem burden will rather lay on the other, the controversial and capitalisation form, which has a whole series of technological procedures. The base is selling the creditor rights below their nominal value to third subjects,

both on the national but namely international level (usually consortiums or banks) for convertible currencies. However, a part of it can also be exchanged in the nominal value for the indebted country currency (usually non-convertible) and used for the precisely limited purposes (Figure 1) – (Evans et al. 2001).

It can be divided into the following operations:

- capitalisation or conversion into the portfolio and other investments (debt-for-equity Swaps)
- capitalisation or conversion of the development obligations (debt-for-development swaps)
- capitalisation or conversion of the environmental initiatives (debt-for-nature swaps), the first of which is quite dominant and the other two have only just been started and are still in the embryonic stage.

In the latter two cases, third partners usually are international organisations, either of the charity or NGO type (UNICEF, environmental organisations, UNDP etc.). It therefore regards the activities of the so-called secondary market with debts, other obligations as well as promises or quotas of the development aid and the contributions on the environmental projects.

Debt obligations are then traded in the secondary market with discounts reaching 30–80% of the nominal value. At present, the general tendency rather is decreasing of the discounts, namely if they are secured through the government bonds of some DMEs, namely the U.S. ones (so-called Brady’s bonds). Very poor and hopelessly indebted countries will not find any interested buyers even in the secondary market. Similarly, the above described capitalisation techniques are rather suitable for the long-term loans and governmental credits and little suitable for commercial credits, not even for those having some form of the state guarantee. Nevertheless, even those guarantees are often regarded as insufficient or not creditable. Typical examples of this are the poor Sub-Saharan countries. The conversion and capitalisation (swap) operations have many advantages, the main of which are the relief of the debt burden, the support of the investment climate and the limited outflow of capital, the export support and substitution of import, the support of privatisation and of private sector in the mixed DCs economies as such. On the other hand, there are mentioned also certain potential disadvantages. Besides the already mentioned risk of creation of the hidden inflation potential on the national and international level, it is also the so-called effect of the additional “saving net” for the payment balance, which is not adequate to the real economic efficiency increase, and finally a certain risk of the uncontrolled and inadequate investment allocation according to the sector structure (Srnc and Svobodová 2009).

Table 3. Debt indicators – developing countries

	1980– 1990	1991– 1995	1996– 2000	2001– 2005	2000	2005	2006	2007
Total debt (\$ billion)								
All countries	892.3	1 627.4	2 192.2	2 538.9	2 256.6	2 739.9	2 983.7	3 357.2
Sub-Saharan Africa	111.0	202.1	221.7	220.5	211.9	216.2	173.5	193.8
North Africa and Middle East	106.1	152.9	155.2	154.2	145.2	148.9	141.3	151.3
South Asia	72.0	143.5	155.8	178.9	160.0	190.7	227.3	240.3
East Asia and Pacific	134.1	344.7	518.1	555.3	497.7	614.1	660.0	715.6
Latin America and the Caribbean	374.5	517.4	714.7	780.6	754.5	747.3	734.5	787.6
Eastern Europe and Central Asia	94.5	266.7	426.7	649.4	487.1	822.7	1 047.0	1 268.5
Total debt as percentage of GNI								
All countries	30.3	38.6	39.3	35.4	38.9	28.4	26.4	24.4
Sub-Saharan Africa	44.5	70.6	69.3	54.3	66.5	37.1	26.2	25.4
North Africa and Middle East	47.5	63.7	44.4	34.5	38.4	26.2	21.9	19.5
South Asia	22.9	37.1	28.3	23.4	26.7	18.8	19.8	17.1
East Asia and Pacific	26.8	37.0	34.2	24.3	29.6	20.2	18.4	16.3
Latin America and the Caribbean	50.3	37.6	37.6	41.0	38.9	30.7	25.8	23.7
Eastern Europe and Central Asia	–	28.0	46.6	48.1	54.9	40.7	43.2	40.9
Total debt as percentage of exports								
All countries	173.6	172.0	141.9	103.2	122.6	73.6	65.8	62.0
Sub-Saharan Africa	180.7	250.2	213.3	143.9	178.9	88.8	59.8	57.8
North Africa and Middle East	165.8	159.0	134.4	86.0	103.7	59.8	49.1	45.9
South Asia	248.7	271.2	178.0	116.9	151.3	80.7	77.6	69.8
East Asia and Pacific	132.1	119.3	98.9	62.2	77.4	43.8	38.2	34.2
Latin America and the Caribbean	288.5	227.2	187.2	151.4	164.2	105.4	86.8	82.5
Eastern Europe and Central Asia	–	128.2	127.5	112.7	128.4	92.6	95.6	94.1
Debt service as percentage of exports								
All countries	21.8	17.5	19.9	16.8	20.2	13.6	12.6	9.7
Sub-Saharan Africa	14.6	13.3	13.9	8.9	11.4	8.3	7.4	5.0
North Africa and Middle East	19.4	19.9	16.7	10.8	12.7	8.7	10.4	6.1
South Asia	22.1	24.8	18.4	14.6	14.6	11.9	7.5	6.9
East Asia and Pacific	19.1	14.5	12.7	9.6	11.4	5.9	5.0	4.3
Latin America and the Caribbean	37.6	25.4	36.1	29.1	38.9	22.8	23.0	15.3
Eastern Europe and Central Asia	–	12.0	15.9	21.3	19.0	21.7	20.0	16.7
Debt service as percentage of GNI								
All countries	4.1	4.0	5.5	5.8	6.4	5.2	5.1	3.8
Sub-Saharan Africa	3.7	3.8	4.5	3.4	4.2	3.5	3.2	2.2
North Africa and Middle East	5.7	8.0	5.5	4.3	4.7	3.8	4.6	2.6
South Asia	2.0	3.4	2.9	2.9	2.6	2.8	1.9	1.7
East Asia and Pacific	3.9	4.5	4.4	3.7	4.3	2.7	2.4	2.1
Latin America and the Caribbean	6.8	4.2	7.4	7.9	9.2	6.6	6.9	4.4
Eastern Europe and Central Asia	–	2.7	5.9	9.1	8.1	9.5	9.0	7.3
Memo item:								
International reserves (\$ billion)								
All countries	136.5	333.8	624.7	1 335.6	691.6	2 053.1	2 701.5	3 718.7
Sub-Saharan Africa	11.6	17.0	29.9	52.7	36.7	84.4	117.6	147.5
North Africa and Middle East	17.6	32.0	48.4	96.0	51.6	134.8	174.1	216.9
South Asia	11.8	22.5	38.6	114.4	47.2	156.7	198.5	277.3
East Asia and Pacific	40.7	116.2	248.6	629.4	283.0	1 020.4	1 315.7	1 856.8
Latin America and the Caribbean	46.1	108.1	163.8	199.8	158.4	257.3	312.8	444.7
Eastern Europe and Central Asia	–	51.2	95.4	243.3	114.7	399.6	582.8	786.1

Source: UNCTAD (2008), p. 172

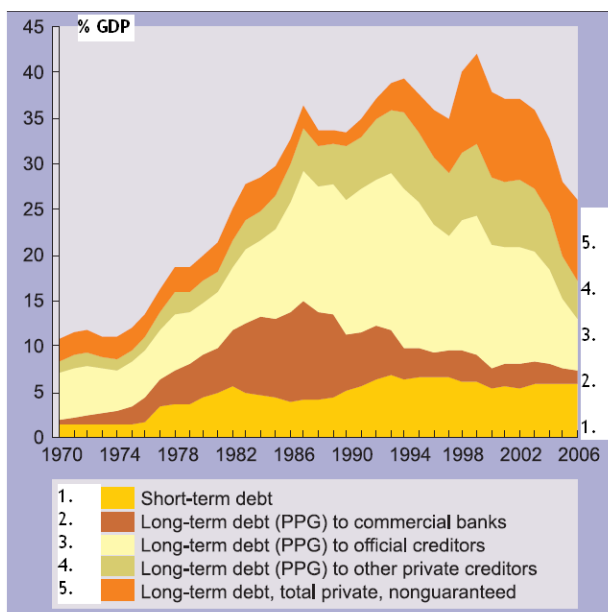


Figure 1: Debts categories (% GDP)

PPG = Public and Publicly Guaranteed Debt

Source: UNCTAD: Trade and Development Report. Geneva 2008, p. 171

The latter disadvantage can be, however, alleviated by the measures on the central bank level towards foreign capital and foreign direct investments on the conversion operations base (subsidies, tax alleviations etc.) (Daland and Srnec 2010).

CONCLUSION

Even if the volume of such operations is growing continually since the mid 80s both regarding the nominal value and the number of included countries, the global problem of international indebtedness still remains the burdening and risk factor of sustaining the world economy stability, but also through it the political and social situation in the world. Even if the general global collapse of the international credit, capital-monetary, and practically even of the whole complex system of world economy, was averted (around 1983), the whole problem is still one of the most dangerous “timed bombs” of the world

economy and politics. It can be gradually liquidated once more only by the world-wide endeavours and in the connection of solving other global problems, namely the change of the system of international relationships, the relationships between the developed and developing countries, and that fully in the sense of the interrelation typical for the whole system of global problems, from which the most typical demonstration is the global poverty problem, both relative and absolute.

REFERENCES

- Amel D., Barnes C., Panetta F., Salleo C. (2004): Consolidation and efficiency in the financial sector: A review of the international evidence. *Journal of Banking and Finance*, 28: 2493–2519.
- Berger A.N. (2003): The economic effects of technological progress: evidence from the banking industry. *Journal of Money, Credit and Banking*, 35: 141–176.
- Dalan G.R., Srnec K. (2010): The scenario of mikrofinance in Latin America against the international financial crisis. *Agricultural Economics – Czech*, 56: 583–590.
- Evans L., Altunbas Y., Molyneux P. (2001): Ownership and efficiency in banking. *Journal of Money, Credit and Banking*, 33: 926–954.
- Srnec K., Svobodová E. (2009). Microfinance in less-developed countries: history, progress, present – charity or business? *Agricultural Economics – Czech*, 55: 467–474.
- Tichá I. (2008). Intellectual capital reporting. *Agricultural Economics – Czech*, 54: 57–62.
- UNCTAD (2008). Trade and Development Report. Geneva.
- World Bank (1995). Debtor Reporting System. Washington.
- World Bank (2001). Global Development Finance 2001. Washington.
- Williams J., Nguyen N. (2005). Financial liberalization, crises and restructuring: a comparative study of bank performance and bank governance in South East Asia. *Journal of Banking and Finance*, 29: 2119–2154.

Arrived on 16th September 2010

Contact address:

Vladimír Jeníček, University of Economics, Prague, Winston Churchill Sq. 4, 130 67 Prague 3, Czech Republic
e-mail: jenicsek@vse.cz
