World Development Report 1985

International Capital and Economic Development
World Development Indicators

World Development Report 1985

Published for The World Bank
Oxford University Press

Oxford University Press
NEW YORK OXFORD LONDON GLASGOW
TORONTO MELBOURNE WELLINGTON HONG KONG
TOKYO KUALA LUMPUR SINGAPORE JAKARTA
DELHI BOMBAY CALCUTTA MADRAS KARACHI
NAIROBI DAR ES SALAAM CAPE TOWN

First printing July 1985

The denominations, the classifications, the boundaries, and the colors used in maps in World Development Report *do not imply on the part of The World Bank and its affiliates any judgment on the legal or other status of any territory, or any endorsement or acceptance of any boundary.*

ISBN 0-19-520481-6 cloth bound
ISBN 0-19-520482-4 paperback
ISSN 0163-5085

The Library of Congress has cataloged this serial publication as follows:
World development report. 1978–
[New York] Oxford University Press.
v. 27 cm. annual.
Published for The World Bank.

1. Underdeveloped areas—Periodicals. 2. Economic development—Periodicals I. International Bank for Reconstruction and Development.

HC59.7.W659 330.9'172'4 78–67086

This book is printed on paper that adheres to the American National Standard for Permanence of Paper for Printed Library Materials, Z39.48-1984.

Foreword

This is the eighth *World Development Report.* It focuses on the contribution that international capital makes to economic development—a topical issue in view of the international concern with external debt over the past several years. While this Report pays close attention to the events of the recent past, it also places the use of foreign capital in a broader and longer-term perspective.

Using such a perspective, the Report shows how countries at different stages of development have used external finance productively; how the institutional and policy environment affects the volume and composition of financial flows to developing countries; and how the international community has dealt with financial crises.

The financial links between industrial and developing countries have become as integral to the world economy as trade has hitherto been. This growing interdependence is a development of profound significance. Just as governments recognize that their trading policies have international consequences, so they are starting to see that the same is true of their financial policies. Their fiscal and monetary policies, rules on foreign borrowing and lending, and attitudes toward foreign investment are not only components of domestic policy, they also determine the efficiency with which world savings are used.

Nothing has better illustrated this new interdependence than the experience of the recent past. Expanded financial flows helped developing countries to sustain high levels of investment and to smooth structural adjustments. When difficulties arose, individual governments, central banks, international agencies, and commercial bankers have contributed to the task of stabilizing the world's financial system. Their approach has been pragmatic, devising remedies according to each country's difficulties. Their efforts have been complemented by the very painful adjustment measures implemented by the debtor countries themselves. More has been achieved than many observers thought possible when the recession was at its trough.

We are now in a period of transition—an essential and intermediate phase before returning to sustained growth and normal relationships between debtors and creditors. A successful transition will require continuing efforts by governments, international agencies, and commercial banks. All participants in the rescheduling exercises of the past three years will need continued patience and imagination to smooth out the hump of repayments in the next five years, when about two-thirds of the debt of developing countries falls due, and to place debt on a sounder longer-term footing.

Stable and noninflationary growth in industrial economies is an essential component of a successful transition. Policies that produce a softening of interest rates and an easing of protectionism would facilitate the developing countries' resumption of growth and the restoration of their creditworthiness, without which they cannot get the extra capital that they need from abroad to promote their development.

How much they obtain will depend largely on their success in restoring creditworthiness, which in turn hinges on the policies they pursue. A recurring theme of this Report is that the countries in debt-servicing difficulties are not necessarily those with the largest debts or those that have suffered the biggest external shocks. A country's ability to borrow and service its foreign debt is largely determined by the quality and flexibility of its policies, its ability to appraise and implement sound investment projects, and by good debt management. Foreign finance is a complement to, and not a substitute for, domestic efforts.

The same basic policy prescriptions apply to every country. However, this Report highlights the particular constraints on countries in sub-Saharan Africa. For the foreseeable future, most African countries will have to continue to rely on concessional aid for the bulk of their external finance. Their needs are great and increasing every year. Linked to policy reforms, additional aid could have a marked impact on halting the decline in living standards, particularly in the poorest countries.

This Report concludes that the developing countries will have a continuing need for external finance. It demonstrates that many of the policies required to attract external finance and promote economic growth are either being implemented or planned already. No government—either in an industrial or a developing country—is being asked to act against its own long-term interests. If each follows the route outlined, all can and will benefit from a more prosperous and stable world. That is the cautiously optimistic conclusion of this Report.

Like its predecessors, this year's *World Development Report* is a study by the staff of The World Bank, and the judgments in it do not necessarily reflect the view of our Board of Directors or the governments they represent.

A. W. Clausen
President
The World Bank

May 24, 1985

This Report was prepared by a team led by Francis Colaço and comprising Alexander Fleming, James Hanson, Chandra Hardy, Keith Jay, John Johnson, Andrew Steer, Sweder van Wijnbergen, and K. Tanju Yürükoğlu, assisted by Oliver Adler, Nadeem Burney, Sandra Gain, Shahrzad Gohari, Tina Jacobsen, Tani Maher, Hossein Ali Partoazam, Kesavan Pushpangadan, and James Rosen. The Economic Analysis and Projections Department, under the direction of Jean Baneth, supplied data for the Report. Enzo Grilli and Peter Miovic coordinated the work of the Economic Analysis and Projections Department on projections. Ramesh Chander, assisted by David Cieslikowski, supervised the preparation of the World Development Indicators; Shaida Badiee was responsible for systems design. The authors would also like to thank staff from various parts of the Bank, as well as other contributors and reviewers. Thanks are also due to the production staff, especially Joyce Eisen, who designed the cover, Pensri Kimpitak, and Carol Cole Rosen. Special thanks go to the support staff, headed by Rhoda Blade-Charest and including Banjonglak Duangrat, Jaunianne Fawkes, Pamela Holmes, Carlina Jones, and Patricia Smith. The work was carried out under the general direction of Anne O. Krueger and Costas Michalopoulos, with Rupert Pennant-Rea as principal editor.

Definitions and data notes

Capital flows

• *Components of capital flows.* International movements of capital may come from either official or private sources. Official sources are (a) governments and governmental agencies (also called *bilateral lenders*) and (b) international organizations (called *multilateral lenders*). Private sources comprise (a) commercial suppliers and manufacturers, which provide export credits for the purchase of their goods, (b) commercial banks, which provide export credits or cash loans, (c) other private investors, who invest in foreign enterprises in which they seek a lasting interest (direct investment) or purchase stocks or bonds issued by foreign companies or governments (portfolio investment), and (d) charitable organizations, which provide financial aid, goods, and services as grants.

• *Concessional flows.* International lending on terms more favorable to the borrower than those obtainable through normal market transactions. In this text, concessional flows are defined as those having a grant element of 25 percent or more.

• *Direct foreign investment.* Investment made to acquire a lasting interest in an enterprise operating in an economy other than that of the investor, the investor's purpose being to have an effective voice in the management of the enterprise.

• *Equity financing.* Investment that confers whole or partial ownership in an enterprise and entitles the investor to share in the profits from its operation. International equity financing flows may be included in either foreign direct or portfolio investment.

• *Export credits.* Finance provided by lenders in a given country for exports of specific goods or services. Conventionally, one distinguishes between private and official export credits. *Private export credits* consist of (a) supplier credits, which are extended by the exporting company to the foreign buyer and (b) buyer credits, which are extended by commercial banks in the exporting country on behalf of the exporters. *Official export credits* are extended by an agency of the exporting country's government.

• *Grant.* A current transfer of capital, goods, or services to a foreign country that results in no current or future obligation to make a like transfer from the recipient country to the donor.

• *Grant element.* The extent to which a loan can be considered a grant is determined by its *grant element*—the difference between the original face value of the loan and the discounted present value of debt service, as a percentage of the original face value. Thus a true grant has a grant element of 100 percent. A discount rate of 10 percent is conventionally used in the calculation. The grant element is used to compare the concessionality of assistance provided under differing terms and conditions.

• *Net flows of lending.* Loan disbursements less amortization of principal.

• *Nonconcessional flows.* Lending on or near terms prevailing in private financial markets.

• *Official development assistance.* Loans and grants made on concessional financial terms from official sources, with the objective of promoting economic development and welfare. It includes the value of technical cooperation and assistance.

• *Private nonguaranteed debt.* Private nonguaranteed loans are external obligations of private debtors that are not guaranteed for repayment by a public entity of the debtor country.

• *Public and publicly guaranteed debt.* Public loans are external obligations of public debtors, including national governments, their agencies, and autonomous public bodies. Publicly guaranteed loans are external obligations of private debtors that are guaranteed for repayment by a public entity of the debtor country.

Trade and finance

• *Balance of payments.* A systematic record of the economic transactions between a nation's residents and nonresidents during a given period, usually one calendar or fiscal year. It covers the flows of real resources (including factor services, such as the services of labor and capital) across the boundaries of the domestic economy, changes in foreign assets and liabilities resulting from economic transactions, and transfer payments to and from the rest of the world. Balance of payments accounts comprise two broad categories: the current account, which measures merchandise trade, factor and nonfactor service income, and transfer receipts and payments, and the capital account, which measures changes in domestic and foreign capital assets and liabilities.

- *Current account balance.* A representation of the transactions that add to or subtract from an economy's stock of financial items. It is given as the sum of net exports of goods and nonfactor services, net factor income, and net transfers. Official capital grants are excluded.
- *Debt reorganization.* Any change in the payment arrangements associated with an existing stock of debt mutually agreed upon by the borrower and the lender. In *debt refinancing,* new loans are negotiated to meet debt service obligations on existing debt. In *debt rescheduling,* arrangements are agreed upon for postponing payments of principal or interest or otherwise changing the terms of repayment or of interest charges.
- *Debt service.* The sum of interest payments and repayments of principal on external debt. The *debt service ratio* is total debt service divided by exports of goods and services.
- *External debt.* Debt that is owed to nonresidents. World Bank data, unless otherwise specified, cover external debt that has an original or extended maturity of one year or more and that is repayable in foreign currency, goods, or services. Transactions with the International Monetary Fund are excluded (with the exception of Trust Fund loans). A distinction in medium- and long-term debt is made between *private nonguaranteed debt* and *public and publicly guaranteed debt.*
- *Interest rates.* The *nominal rate* on a given loan is the percentage stipulated in the loan contract and may be expressed as a *fixed rate,* that is, an interest rate that is constant over the duration of the loan, or as a *variable, or floating, rate,* an interest rate that is recalculated at fixed intervals (such as every six months). Variable interest rates consist of a base rate (such as the six-month London interbank offered rate) plus a margin, or spread. *Market, or world, rates* reflect the terms of borrowing at any given time in private capital markets; market rates are usually differentiated as *long-term rates*—the current rates payable on financial instruments, such as bonds, having maturities of more than one year—and *short-term rates*—those on such instruments maturing in one year or less. The *real interest rate* is the nominal rate adjusted to account for changes in the price level.
- *Intermediation.* The process whereby a private or official financial agency accepts funds from investors and onlends them to borrowers.
- *Maturity.* For a loan, the date at which the final repayment of principal is to be made. *Short-term loans* are those with original maturity of a year or less; *medium- and long-term loans* are those with original or extended maturity of more than one year.
- *Reserves.* A country's international reserves comprise its holdings of monetary gold and special drawing rights; its reserve position in the International Monetary Fund; its holdings of foreign exchange under the control of monetary authorities; its use of IMF credit; and its existing claims on nonresidents that are available to the central authorities. Reserves are also expressed in terms of the number of months of imports of goods and services they could pay for.
- *Resource balance.* The difference between exports of goods and nonfactor services and imports of goods and nonfactor services.
- *Spread.* The difference between a reference rate used to price loans and the rate at which funds are lent to final borrowers. A widely used reference rate is the London interbank offered rate, or LIBOR—the rate at which banks participating in the London market are prepared to lend funds to the most creditworthy banks. Another is the U.S. prime rate.
- *Terms of trade.* A measure of the relative level of export prices compared with import prices. Calculated as the ratio of a country's index of export unit value to the import unit value, this indicator shows changes over a base year in the level of export prices as a percentage of import prices.
- *Trade balance.* The difference between merchandise exports f.o.b. and merchandise imports f.o.b.

National accounts

- *Gross domestic product.* The total final output of goods and services produced by an economy—that is, by residents and nonresidents, regardless of the allocation to domestic and foreign claims. It is calculated without making deductions for depreciation.

- *Gross national product.* The total domestic and foreign output claimed by residents. It comprises gross domestic product adjusted by net factor income from abroad. Factor income comprises receipts that residents receive from abroad for factor services (labor, investment, and interest) less similar payments made to nonresidents abroad. It is calculated without making deductions for depreciation.
- *Investment.* The sum of gross domestic fixed investment and the change in stocks (or inventories). Gross domestic investment covers all outlays of the private and public sectors for additions to the fixed assets of the economy, plus the value of change in stocks (or inventories).
- *Savings.* Gross domestic savings is defined as the difference between GDP and total consumption, and gross national savings are obtained by adding net factor income from abroad and net current transfers from abroad to gross domestic savings.

Country groupings

- *Developing countries* are divided into: *low-income economies,* with 1983 gross national product (GNP) per person of less than \$400; and *middle-income economies,* with 1983 GNP per person of \$400 or more. Middle-income countries are also divided into *oil exporters* and *oil importers,* identified below.
- *Middle-income oil exporters* comprise Algeria, Angola, Cameroon, People's Republic of the Congo, Ecuador, Arab Republic of Egypt, Gabon, Indonesia, Islamic Republic of Iran, Iraq, Malaysia, Mexico, Nigeria, Peru, Syrian Arab Republic, Trinidad and Tobago, Tunisia, and Venezuela.
- *Middle-income oil importers* comprise all other middle-income developing countries not classified as oil exporters. A subset, *major exporters of manufactures,* comprises Argentina, Brazil, Greece, Hong Kong, Israel, Republic of Korea, Philippines, Portugal, Singapore, South Africa, Thailand, and Yugoslavia.
- *High-income oil exporters* (not included in developing countries) comprise Bahrain, Brunei, Kuwait, Libya, Oman, Qatar, Saudi Arabia, and United Arab Emirates.
- *Industrial market economies* are the members of the Organisation of Economic Co-operation and Development, apart from Greece, Portugal, and Turkey, which are included among the middle-income developing economies. This group is commonly referred to in the text as industrial economies or industrial countries.
- *East European nonmarket economies* include the following countries: Albania, Bulgaria, Czechoslovakia, German Democratic Republic, Hungary, Poland, Romania, and USSR. This group is sometimes referred to as *nonmarket economies.*
- *Sub-Saharan Africa* comprises all thirty-nine developing African countries south of the Sahara, excluding South Africa, as given in *Toward Sustained Development in Sub-Saharan Africa: A Joint Program of Action* (World Bank 1984).
- *Middle East and North Africa* includes Afghanistan, Algeria, Arab Republic of Egypt, Iran, Iraq, Israel, Jordan, Kuwait, Lebanon, Libya, Morocco, Oman, Saudi Arabia, Syrian Arab Republic, Tunisia, Turkey, Yemen Arab Republic, People's Democratic Republic of Yemen, and United Arab Emirates.
- *East Asia* comprises all low- and middle-income countries of East and Southeast Asia and the Pacific, east of, and including, Burma, China, and Mongolia.
- *South Asia* includes Bangladesh, Bhutan, India, Nepal, Pakistan, and Sri Lanka.
- *Latin America and the Caribbean* comprises all American and Caribbean countries south of the United States.
- *Major borrowers* are countries with disbursed and outstanding debt estimated at more than \$15 billion at the end of 1983 and comprise Argentina, Brazil, Chile, Egypt, India, Indonesia, Israel, Republic of Korea, Mexico, Turkey, Venezuela, and Yugoslavia.

Acronyms and initials

BIS Bank for International Settlements.
DAC The Development Assistance Committee of the Organisation for Economic Co-operation and Development comprises Australia, Austria, Belgium, Canada, Denmark, Finland, France, Federal Republic of Germany, Italy, Japan, Netherlands, New Zealand, Norway, Sweden, Switzerland, United Kingdom, United States, and Commission of the European Communities.
EC The European Communities comprise Belgium, Denmark, France, Federal Republic of Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, and United Kingdom.
FAO Food and Agriculture Organization.

GATT General Agreement on Tariffs and Trade.
GDI Gross domestic investment.
GDP Gross domestic product.
GDS Gross domestic savings.
GNP Gross national product.
GNS Gross national savings.
IBRD International Bank for Reconstruction and Development.
IDA International Development Association.
IFC International Finance Corporation.
ILO International Labour Office.
IMF International Monetary Fund.
LIBOR London interbank offered rate.
NGO Nongovernmental organization.
ODA Official development assistance.
OECD The Organisation for Economic Co-operation and Development members are Australia, Austria, Belgium, Canada, Denmark, Finland, France, Federal Republic of Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, United Kingdom, and United States.
OPEC The Organization of Petroleum Exporting Countries comprises Algeria, Ecuador, Gabon, Indonesia, Islamic Republic of Iran, Iraq, Kuwait, Libya, Nigeria, Qatar, Saudi Arabia, United Arab Emirates, and Venezuela.
SDR Special drawing right.
UN United Nations.
UNCTAD United Nations Conference on Trade and Development.
UNDP United Nations Development Programme.
Unesco United Nations Educational, Scientific, and Cultural Organization.
UNICEF United Nations Children's Fund.

Data notes

Billion is 1,000 million.
Tons are metric tons (t), equal to 1,000 kilograms (kg) or 2,204.6 pounds.
Growth rates are in real terms unless otherwise stated. Growth rates for spans of years in tables cover the period from the beginning of the base year to the end of the last year given.
Dollars are current U.S. dollars unless otherwise specified.
The symbol . . in tables indicates data are not available.

All tables and figures are based on World Bank data unless otherwise specified. Throughout this volume, unless otherwise noted, World Bank data on debt cover medium- and long-term public and publicly guaranteed plus private nonguaranteed debt outstanding and disbursed. Data on short-term debt have been estimated by World Bank staff from the published semiannual series of the Bank for International Settlements on the maturity distributions of international lending; adjustments to the BIS data have been made to exclude known amounts that have been rolled over into long-term debt during reschedulings. The World Development Indicators at the back of this volume use the country groupings given above but include only countries with a population of 1 million or more.

Data from secondary sources are not always available through 1983. The numbers in this *World Development Report* shown for historical data may differ from those shown in previous Reports because of continuous updating as better data become available, and because of recompilation of certain data for a ninety-country sample. The recompilation was necessary to permit greater flexibility in regrouping countries for the purpose of making projections.

Contents

Part IV Perspectives and Policies for the Future

World Development Indicators 163

Text tables

Appendix tables

Text figures

Boxes

Part I Overview and Historical Perspective

1 Overview

The economic turbulence of the past few years has subsided. The recovery of industrial economies in 1983–84, policy adjustments by many developing countries, and flexibility by commercial banks in dealing with debt-servicing difficulties have all helped to calm the atmosphere of crisis. This does not mean, however, that the world economy has regained its momentum of the 1960s or that development is again making rapid progress. Growth has slowed in most developing countries that experienced debt-servicing difficulties and in many of those that did not. Average per capita real incomes in most of Africa are no higher than they were in 1970; in much of Latin America, they are back to the levels of the mid-1970s. Dozens of countries have lost a decade or more of development.

The experience of the past few years has raised many questions about the role of international capital in economic development. Only a few years ago, there was general agreement that the more advanced developing countries could and should borrow more commercial capital from abroad. That consensus has been broken. Some people believe that the case by case approach to addressing debt difficulties is creating a sustainable balance of growth and debt servicing that will in time encourage more lending, including bank lending. Others believe that new approaches are needed if developing countries are to service their debt and resume economic growth. As with so many changes in conventional wisdom, both new and old arguments are often stylized and exaggerated. It is important not to lose sight of the fundamentals of international finance.

Capital has long flowed from richer to poorer countries. It has done so because it is relatively scarcer in economies that are at earlier stages of development, and the expected rates of return tend to be correspondingly higher. What is at issue is the nature of capital flows, their terms, and their uses. These questions were relevant in the nineteenth century and remain so today.

This Report offers a broad and long-term perspective on the role of international capital in economic development. It emphasizes that international flows of capital can promote global economic efficiency and can allow deficit countries to strike the right balance between reducing their deficits and financing them. The availability of international capital also involves risks, however: first, that it may delay the policy reforms required for adjustment; and second, that countries may borrow too much if they misjudge the way in which external economic conditions are going to evolve.

Both benefits and costs can be illustrated by recent experience. On the benefits side, most developing countries have made substantial economic progress over the past twenty years. Their GDP growth averaged 6.0 percent a year in 1960–80. The life expectancy of their people rose from an average of forty-two years in 1960 to fifty-nine years in 1982, while infant mortality was halved and the primary school enrollment rate rose from 50 to 94 percent. These advances reflected principally the efforts of developing countries themselves. But there is considerable evidence that capital flows, often accompanied by technical know-how, have played a part.

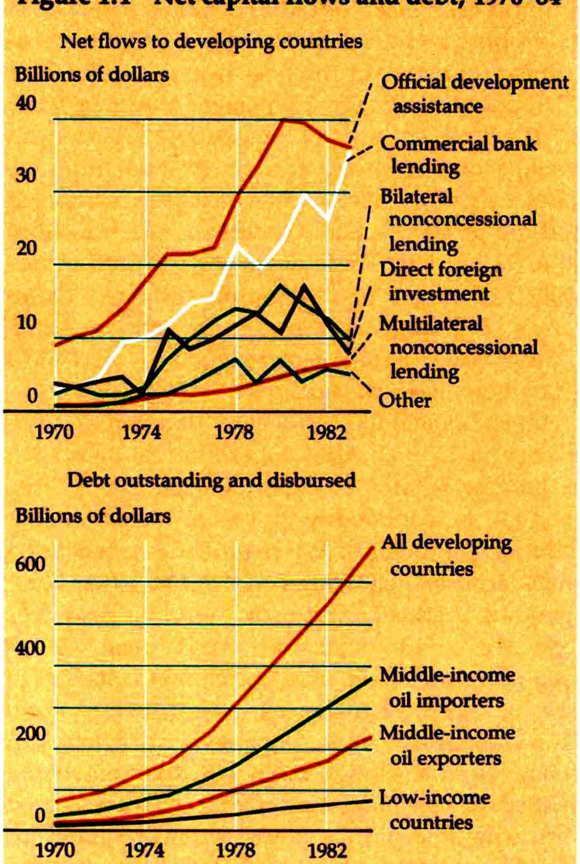
Foreign capital has also helped individual countries to cushion shocks—either internal ones such as harvest failures or external ones such as big changes in commodity prices or recessions in industrial economies. External finance can act as a shock absorber, allowing countries to adjust their spending gradually and reallocate their resources for a new environment. In the 1970s many developing countries were able, in the first instance, to pay for more expensive oil by borrowing more. Those countries that accompanied borrowing with policy reforms restored rapid growth and avoided debt-servicing difficulties. Other countries used borrowing to avoid the policy actions required for adjustment. Many of them ran into debt-servicing problems and needed to take even more drastic and costly adjustments later.

This contrast emphasizes that foreign borrowing is not a painless or riskless alternative to adjustment. The accumulation of debt makes a country more susceptible to international financial fluctuations, as the swing from negative real interest rates to unprecedentedly high positive rates has made all too plain. The need for rapid adjustment increased. Borrowers and lenders often fail to take full account of the institutional, social, and political rigidities that restrict a country's capacity to adjust.

The historical context

The ten years 1973–82 saw a big increase in the foreign finance going to developing countries. As a result, both the gross and net debt of developing countries increased sharply. Between 1970 and 1984 the outstanding medium- and long-term debt of developing countries expanded almost tenfold, to $686 billion (see Figure 1.1), despite the decline in capital flows since 1981. The most striking feature of this growth was the surge in lending by commercial banks. Their share of total new flows to developing countries increased from 15 percent in 1970 to 36 percent in 1983.

Figure 1.1 Net capital flows and debt, 1970–84



Source: For net flows: OECD *Development Co-operation;* for debt: World Bank data.

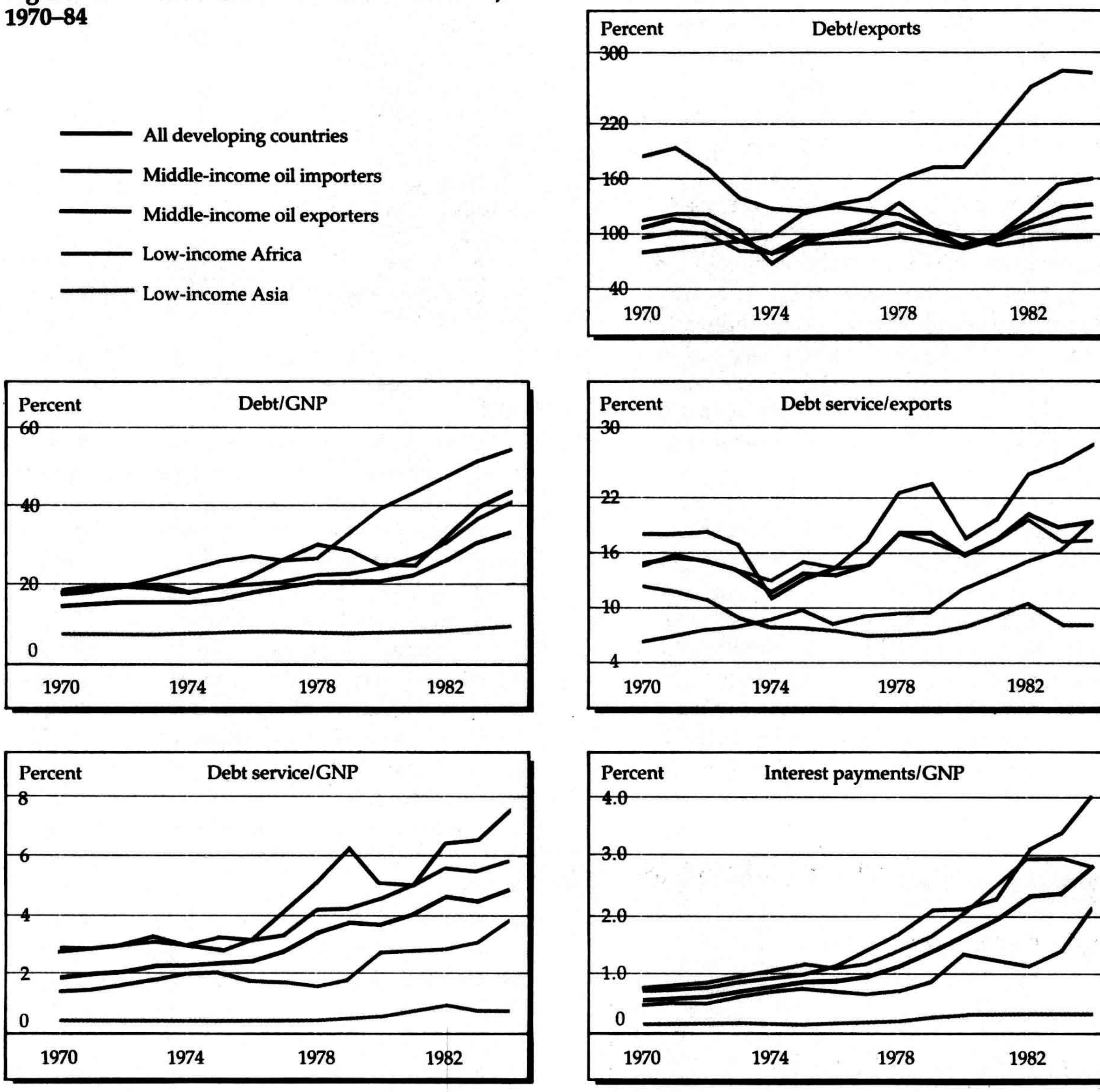
On every measure, the debt-servicing abilities of developing countries deteriorated, particularly after 1974, as their debt increased (see Figure 1.2). The ratio of debt to GNP more than doubled, from 14 percent in 1970 to almost 34 percent in 1984. The ratio of debt service to exports rose from 14.7 percent in 1970 to a peak of 20.5 percent in 1982, declining to 19.7 percent in 1984. Interest payments on debt increased from 0.5 percent of GNP in 1970 to 2.8 percent of GNP in 1984 and accounted for more than half of all debt service payments in that year. These averages conceal wide regional and country differences.

Dramatic though the recent growth of foreign borrowing has been, it is not unprecedented. As Chapter 2 makes clear:

• The volume of international capital flows has often been larger in relative terms than in the 1970s. Between 1870 and 1913, Great Britain invested an average of 5 percent of its GNP abroad, rising to almost 10 percent just before World War I. For France and Germany, the figure was 2 to 3 percent of GNP. As a proportion of the recipient country's GNP, capital inflows were also often larger in earlier periods. Inflows to Canada, for example, averaged 7.5 percent of its GNP between 1870 and 1910 and accounted for 30 to 50 percent of its domestic investment. During the investment booms in Argentina and Australia, foreign capital was roughly half of all gross domestic investment. By contrast, net capital inflows to all developing countries averaged 2 to 3 percent of their GNP between 1960 and 1973, while financing 10 to 12 percent of their gross investment; since then, net capital inflows have been between 3 and 6 percent of their GNP and have financed 10 to 20 percent of their gross investment.

• The structure of financial flows to developing countries has changed several times. In the years before World War I, private bond markets were the main source of capital. In the 1930s, following the Great Depression and widespread defaults by borrowers in both industrial and developing countries, commercial lending to developing countries virtually stopped. It was replaced after World War II by an expansion of official flows, mainly on concessional terms; the largest part was bilateral aid, but some was channeled through the new multilateral agencies such as the World Bank and later the

Figure 1.2 Trends in selected debt indicators, 1970–84



Note: Interest and debt service for 1970–83 are actual (not contractual) service paid during the period. Interest and debt service for 1984 are projections of contractual obligations due based on commitments received through the end of 1983 and take into account reschedulings through the end of 1984.

Source: World Bank data.

International Development Association. Along with private direct investment and supplier credits, official finance provided the bulk of external capital for developing countries until the late 1960s, when commercial banks started to play a prominent role.

- Debt-servicing difficulties have been common and usually have been caused by a combination of poor domestic policies and a deteriorating world environment. The fifty years before World War I saw several debt repudiations, including the Peruvian and Turkish crises in the 1870s and the Argentinian and Brazilian crises of the 1880s and 1890s. Defaults, however, were not confined to developing countries: some borrowers in the United States, for example, defaulted on their debts in these years. In the 1930s defaults were widespread, starting with Germany in 1932. Argentina was the only country in Latin America to service its debt on the terms contracted during these years. Except in the 1930s, countries were able to resume borrowing (albeit on more expensive terms) once they had reformed their policies.

By historical standards, debt-servicing difficulties in the 1960s and 1970s do not seem unduly serious. In 1955–70 seven developing countries (Argentina, Brazil, Chile, Ghana, Indonesia, Peru, and Turkey) were involved in seventeen debt reschedulings. There were also some debt reschedulings for low-income countries, including India, but these were designed to provide additional finance when official lenders could not increase new lending. In the 1970s, despite the sharp fall in their terms of trade in 1973–74, an average of three developing countries a year rescheduled their debts.

It is only in the 1980s that debt problems have multiplied. The number of reschedulings rose to thirteen in 1981 and to thirty-one (involving twenty-one countries) in 1983 and a similar number in 1984 (see Figure 1.3). Countries have restructured their repayment schedules, sometimes for several years at a time, in the context of agreed upon programs of policy reform. Low-income countries, however, particularly in Africa, have yet to benefit from the kind of multiyear rescheduling that some major debtors have negotiated.

Table 1.1 Composition and terms of capital flows to developing countries in selected periods

Component and term	*1960–65*	*1975–80*	*1980–83*
Direct foreign investment as a percentage of net capital flows	19.8	15.5	12.9
Floating interest rate loans as a percentage of public debt	. .	26.5	37.9
Average years maturity on new public debt commitments	18.0	15.0	14.0

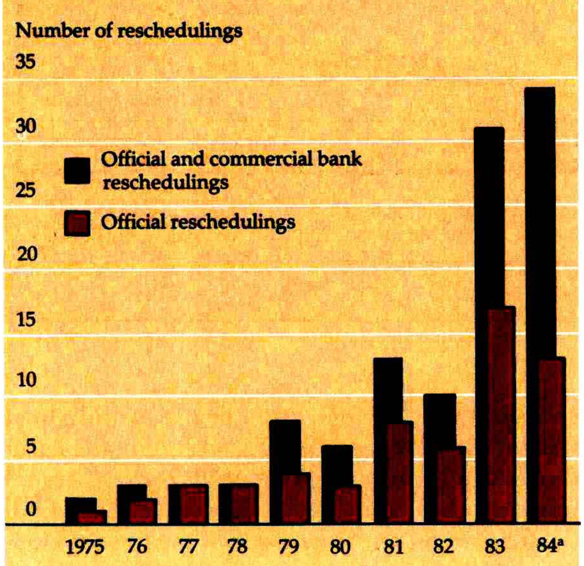
Source: For investment: OECD *Development Co-operation*; for terms: World Bank data.

The similarities with the past should not obscure some differences as well. Developing countries have become more vulnerable to debt-servicing difficulties for three related reasons. First, loans have far outstripped equity finance. Second, the proportion of debt at floating interest rates has risen dramatically, so borrowers are hit directly when interest rates rise. Third, maturities have shortened considerably, in large part because of the declining share of official flows and debt—and by even more than Table 1.1 suggests, if account is taken of the way in which higher inflation and interest rates have front-loaded repayments.

Another major and disturbing difference today is that many of the countries with debt-servicing difficulties are in the low-income group. This is partly because their aid receipts have been erratic. The dollar value of receipts of net official development assistance (ODA) by all developing countries in 1975 was two and a half times the level in 1970, stagnated between 1975 and 1977, almost doubled between 1977 and 1980, and has declined since then. In real terms the pattern is similar, but the fluctuations are less marked. This pattern is explained by variations in bilateral ODA, particularly flows from OPEC countries, since multilateral ODA increased steadily between 1973 and 1980 and has declined only slightly since then. Many low-income and lower-middle-income countries borrowed commercially and accumulated large amounts of debt. In earlier periods, the poorest countries had obtained virtually all their foreign capital in the form of direct investment, especially for export-earning activities, or official flows on concessional terms.

The historical perspective reveals certain broad characteristics of debt-servicing problems. The financial links between industrial and developing

Figure 1.3 Multilateral debt reschedulings, 1975–84



a. Data include commercial bank reschedulings agreed to in principle but not signed as of the end of 1984.

Source: World Bank data.