Finance and Development

The Role of International Commercial Banks in the Third World

Michael DaCosta

A Westview Replica Edition

Finance and Development
The Role of International Commercial Banks in the Third World

Michael DaCosta

Westview Press / Boulder, Colorado

To My Parents, Irene and Philbert.

A Westview Replica Edition

All rights reserved. No part of this publication may be reproduced or transmitted in any form or by any means, electronic or mechanical, including photocopy, recording, or any information storage and retrieval system, without permission in writing from the publisher.

Copyright © 1982 by Westview Press, Inc.

Published in 1982 in the United States of America by
Westview Press, Inc.
5500 Central Avenue
Boulder, Colorado 80301
Frederick A. Praeger, President and Publisher

Library of Congress Cataloging in Publication Data
Finance and development
(A Westview replica edition)
Bibliography: p. 146
1. Unerdeveloped areas--Finance. 2. Underdeveloped areas--Banks and banking. 3. Underdeveloped areas--Financial institutions, International.
I. Title. II. Series.
HG195.D32 1982 332.1'53'091724 82-20276
ISBN 0-86531-917-0

Printed and bound in the United States of America

10 9 8 7 6 5 4 3 2 1

Acknowledgments

Many debts have been incurred in the production of this book. Perhaps the greatest is due to the Bank of Guyana for granting me study leave to pursue the research.

In its formation stages, Helen Agard and Deoranee Budhram were especially helpful in the search for data and other sources. As the work progressed, the librarians at the Bank, at The Institute of Bankers, London, and at UWIST provided valuable references.

Professor Glyn Davies, of the University of Wales (UWIST), deserves special thanks for many helpful comments and guidance throughout the research. Thanks are also due to Professor Gethyn Davies and Nigel Allington of UWIST for the useful discussions which I had with both on the issues arising out of the work.

The manuscript was patiently and meticulously typed by Cecelia France despite the presence of several barely-intelligible passages.

A final debt is due to my wife and parents for providing much encouragement and support throughout the research period.

Michael DaCosta
Georgetown, 1982

Abbreviations

BIS	Bank for International Settlements
DAC	Development Assistance Committee (of the OECD)
GATT	General Agreement on Tariffs and Trade
IBRD	International Bank for Reconstruction and Development - (The World Bank)
IDA	International Development Association
IDB	Inter-American Development Bank
IMF	International Monetary Fund
LDC	Less-Developed Country
LIBOR	London Inter-Bank Offered Rate
OECD	Organization for Economic Cooperation and Development
OPEC	Organization of Petroleum Exporting Countries
UNCTAD	United Nations Conference on Trade and Development
USAID	United States Agency for International Development

试读结束，需要全本PDF请购买 www.ertongbook.com

Contents

List of Tables . . . . *viii*
Acknowledgments . . . . *ix*
Abbreviations . . . . *x*

1. Introduction 1
2. Theoretical Approaches to Growth and Development in Developing Countries 7
3. The Historical Role of Financial Institutions in the Growth of Developing Nations 25
4. The Current Need for External Financial Resources in Developing Countries 31
5. Sources of External Finance to Developing Countries 39
6. Banks as a Source of External Finance in Non-Oil LDCs 66
7. The Contribution of International Banking to Growth in Non-Oil Developing Countries . . . 73
8. Some Criticisms of the Role of International Banks in Financing the Non-Oil LDCs 85
9. The Importance of Appropriate Domestic Economic Policies in Complementing the Contribution of the International Banks 96
10. The Financing Needs of the Least-Developed Countries 114
11. Conclusion 122

Appendix *127*
Notes to Chapters *134*
Bibliography *146*
Index *160*

Tables

4.1 Growth of Gross Domestic Product and Gross Domestic Product Per Capita 1960-80 35
4.2 Non-Oil Developing Countries: Current Account Financing 1973-82 36
5.1 Import Financing of Non-Oil Developing Countries 1973-82 40
5.2 Total Net Resource Receipts of Developing Countries 1971-80 47
5.3 Use of IMF's General Resources by Non-Oil LDCs 51
5.4 Bank and IDA: Trends in Lending, By Sector . . 58
5.5 Bond Issues by Selected Non-Oil LDCs, 1975-81 63
6.1 Sources of New Funds in the Eurocurrency Credit Market 72
7.1 Bank Lending to Non-Oil Developing Countries, 1976-81 76
7.2 Selected International Bank Loans to Developing Countries, 1978 to Second Quarter 1979 . . 77
8.1 Percentage Distribution of Spreads over Inter-Bank Rates Charged to Developing-Country Borrowers 90
8.2 Percentage Distribution of Maturities on Bank Loans to Developing Countries 92

1 Introduction

The task of achieving rates of economic growth sufficient to improve the standards of living of the people of non-oil less-developed countries continues to be of prime concern to policymakers both within and outside the developing regions. This task is indeed monumental. For example, recent estimates show that by the year 2000, some six to seven hundred million people could be living in absolute poverty.[1)] To merely maintain the existing standards of living, a rate of growth of at least 2.5 per cent, equivalent to the average rate of population growth, would need to be achieved.

Growth requires resources of all kinds - human, material and financial. Few developing countries have had the internal capacity to generate sufficient levels of financial resources to satisfy the requirements of growth. As a group, therefore, they have had to supplement their domestic savings with large flows of external grants and loans. In the years immediately following the end of the Second World War and in the wake of the apparent success of the Marshall Plan in Europe, bilateral aid was widely regarded as the solution to the resource gap faced by the developing nations. However, after many years of experience with this type of assistance, disappointment with the contribution of official aid to growth is now widespread. As a result,

several plans have been advanced for increasing the volume and quality of external flows to the less-developed countries. Among these are:-

1. the SDR-aid link proposal,
2. the creation of a special institution to finance exploitation of minerals and other natural resources in LDCs, and
3. a guarantee scheme to facilitate access of developing countries to the international capital markets.

While much work continues on attempting to effect these and other proposals, multilateral and regional financial institutions have, especially in the past two years, adopted several measures aimed at raising the level of assistance to LDCs. At the International Monetary Fund, the Compensatory Financing Facility, designed to assist countries in meeting the balance of payments consequences of export shortfalls due to external factors, has been broadened to include shortfalls in travel receipts and workers remittances. In addition, the facility may now be used to compensate member countries for increased costs of cereal imports. Also, the Fund has moved into the area of medium to long-term balance of payments financing with its agreement to extend the repayment periods under its enlarged facilities to ten years. At the World Bank the introduction of the Structural Adjustment programme, and emphasis on the energy sector and on co-financing have been important recent developments. Finally, regional development banks have devoted much effort to mobilizing larger flows of external finance for their respective areas.

In spite of these efforts and initiatives, it seems clear that the official sector of the international monetary system has failed to meet the growing financial needs of the LDCs especially in the wake of the two

"oil crisis" periods of 1973-1974 and 1978-1979. Nevertheless it was over these periods that unprecedented rates of growth were recorded by developing countries largely as a result of balance of payments and development finance provided by international commercial banks.

A properly functioning international monetary system is one which ideally:

> ...provides a combination of international liquidity and adjustment mechanisms adequate to permit rectification of balance of payments disequilibria without imposing the necessity of severely deflationary policies on the deficit countries or obliging them to resort to balance of payments restrictions on current and capital account transactions, and over the long run provides a rate of increase of international liquidity adequate to support a steady growth of world production, trade and payments at levels as close to 'full-employment' of world resources as possible.[2]

While the I.M.F. has focussed primarily on adjustment mechanisms, the international commercial banks have shown themselves to be sufficiently innovative and flexible to enable the world financial system to overcome two major disturbances. This book stresses the role of the banks not only because of their critical importance during the oil crises and their aftermath, but also because it is felt that the contribution of international banks to economic development has been underestimated in both the literature on economic growth and by policymakers in the LDCs.

Since the thirteenth and fourteenth centuries, banks and bankers have played a crucial role not only in the development of their own countries but also in that of foreign lands. Their importance in domestic financial intermediation has long been recognized in both theory and economic policy, but their potential for transferring resources internationally from surplus to deficit countries has until recently been largely ignored. That

banks should now perform on a global scale a task so well done domestically, is not surprising given the degree of interdependence in the world economy - in turn a result of the ease and speed of international communications and the growing internationalization of business.

It is argued here that LDCs will forgo higher levels of growth, with all that it implies, for the welfare of their people unless they make a concerted effort to tap this large source of international savings. Traditional sources of external finance have proven incapable of providing the volume of funds required by the developing countries, and new proposals for larger flows seem unlikely to be implemented in the near future. In such a situation, these countries face the following options:-

1. to plead with donors for additional aid,
2. to try to expand their foreign exchange earnings from exports of goods and services, and
3. to seek additional sources of funds.

In a period of high inflation and generally tight fiscal policies in the donor countries, option 1. seems to hold little prospect for success in spite of much promising and good intentions on the part of the donors. In the long run, option 2. is clearly the most appropriate, but export diversification to maximize foreign exchange earnings requires financing. By tapping world-wide savings held in the international commercial banks and investing them in viable, export-oriented schemes, the less developed countries can aspire to a faster rate of economic growth, the benefits of which could improve the welfare of hundreds of millions of people in the Third World.

Chapter 2 presents an analysis of the relevance of popular growth models to developing countries. It looks particularly at those models in which savings and financial intermediation have a central role in promoting

试读结束，需要全本PDF请购买 www.ertongbook.com

economic growth. From this basis, a simple analytical framework is developed showing how the international financial intermediary role of banks can, by reducing both the foreign exchange and the savings constraints, increase the rate of growth of output and incomes in LDCs. Chapter 3 reviews the historical role played by banks in developing countries while Chapter 4, considers the current need for savings in these countries emphasizing the serious need for external savings. Having established this need, Chapter 5 proceeds to examine the various non-bank sources of external funds available to LDCs. These include bilateral and multilateral aid, the international monetary institutions, and suppliers credits and other shorter-term sources of trade finance. Since the international commercial banks are the major supplier of external funds to the developing countries, Chapter 6 is devoted to an examination of the banks as a source of medium-term finance. Chapter 7, which is the core of the book, examines the direct and indirect contribution of bank lending to the LDCs. It is concluded that by virtue of the sheer volume of lending combined with the many advantages of largely untied funds, this contribution has been substantial.

An examination of the role of international banking would not be complete without a mention of the many criticisms levelled against bank lending for balance of payments and development purposes. It is to this issue that Chapter 8 turns. An important conclusion from the evaluation is that many debt problems attributed to bank lending per se are more accurately the result of inefficient domestic policies. Consequently, Chapter 9 examines the vital role of economic management in complementing the benefits to be derived from borrowing from the banks.

In recognition of the special problems being faced

by the poorest of the less-developed countries, the penultimate chapter briefly depicts the problems and looks at some proposals to increase the flow of concessional assistance. These include the SDR-aid link proposal and the guarantee scheme to facilitate LDC access to the international capital markets. Chapter 11 incorporates some thoughts on the present and future role of international banking in the provision of funds to the developing countries.

2
Theoretical Approaches to Growth and Development in Developing Countries

Theoretical concern with the issue of economic growth was expressed by the early classical economists such as Adam Smith, David Ricardo, and T.R. Malthus. For them, growth was a function of capital formation out of profits with the major limitation being diminishing returns to land and labour.

THE HARROD-DOMAR APPROACH

It was not until the period after the Great Depression of 1929-30, with its massive unemployment of labour, closed factories, and general stagnation of economic activity that the importance of growth resurfaced in the work of economists. The Keynesian Revolution had already shown that it was possible for the economy to stabilize at a less-than-full-employment position because of an inadequate level of aggregate demand. In the Keynesian, tradition, therefore, Harrod was concerned with determining the rate of growth required from one period to the next that would be sufficient to maintain the full-employment level. Unless such a rate of growth of national income was achieved, labour and the productive capacity of the economy would be unemployed or under-utilized. In seeking the more important factors on which growth depends, Harrod and Domar isolated two: firstly, the addition to output as a result of an increment in the capital stock - the incremental capital/output ratio, and

secondly, the marginal propensity to save out of income.[1]

Algebraically, where Y is national income, I is investment, K is capital, S is savings, the savings ratio, $S = S/Y$, and the capital/output ratio K is $\Delta K/\Delta Y$, the model proceeds as follows:

$$\Delta K = I$$
$$K = \frac{\Delta K}{\Delta Y} = \frac{I}{\Delta Y}$$

Now the Growth rate $G = \Delta Y/Y$

Since $I = S$

$$S = I/Y$$
$$K = I/\Delta Y$$
$$\therefore \Delta Y/Y = S/K$$
$$\therefore G = \frac{S}{K}$$

or the rate of growth of output equals the marginal propensity to save divided by the capital-output ratio. It could be increased either by raising the savings ratio or by increasing the efficiency of capital.

In spite of the model's rather restrictive assumptions of savings as a stable proportion of income, fixed capital and labour-output ratios, the absence of technical progress or a foreign sector, the existence of a single, homogenous and well-behaved production function, and full-employment, it has been widely used by planners in developing countries. The usual procedure is to set a target rate of growth for the economy and to divide that figure by an estimated capital-output ratio, obtaining the required savings ratio. Fiscal measures are then implemented to extract part of the required savings from nationals, and foreign aid agencies and commercial sources are approached to provide the remainder.

The attempt to apply fairly short-run Keynesian economics in general, and the Harrod-Domar model of growth in particular is not surprising since many LDC planners and policy-makers were trained overseas in the Harrod-Domar model and Keynesian economics, and in the absence of an

alternative theoretical framework it was quite natural to apply this training on their return home. However, the limited relevance of a model designed for the short-run stabilization of a highly-industrialized economy like Britain to a poor agricultural or mineral-based country must also not be surprising. In reading the work of Harrod or Keynes one fails to see any serious consideration of the developing countries; it seems clear that it was not their intention that the models which they developed should be applied to these countries.[2)]

It takes only a casual observation of all but the newly-industrializing LDCs to discover that the assumptions of the Harrod-Domar model are far from appropriate, or as Reynolds states,

"...verge on a fantasy."[3)]

The almost single-minded emphasis on physical capital in the post World War II period, and in the model is understandable given the rapid recovery in Western Europe in the wake of large amounts of Marshall Aid. The success of the scheme led some economists, including the growing breed of "aid-experts" to advocate aid tied to physical capital as the most important factor in promoting growth in the developing countries. The consequent neglect of land, the agricultural sector, and labour has proved disastrous for the growth prospects of many countries which are only now trying to correct such mistakes.

From the point of view of financial policy, whereas the model treats savings as a stable proportion of income, research into the savings behaviour of LDCs reveals that much potential exists for increasing the average and marginal propensities to save given the high degree of thrift practised by farmers and peasants, the yet under-developed nature of banking systems, unfamiliarity with financial assets as against physical assets, and the usually wide but unused scope for an active interest-rate policy to

attract potential savers. Finally, the model refers to a closed economy when, in fact, trade and capital movements are vital for growth in the developing countries.

In spite of the assumptions however, the Harrod-Domar model is useful in highlighting two important elements in the growth process of developing countries: the need for savings, and for utilizing as efficiently as possible, scarce capital resources. This remains its essential contribution to the theory of growth in developing countries.

THE NEO-CLASSICAL SCHOOL

The rigid assumptions of the Harrod-Domar model, especially fixed capital and labour output ratios, led neo-classical economists, one of the first of whom was Solow, to investigate models containing flexible factor proportions and factor prices.[4)] The result was Solow's use of the Cobb-Douglas production function:

$$Y = \partial K^{\alpha} L^{\beta}$$

where Y, K and L are output, the capital stock, and labour, ∂ is a constant - indicating the state of technical progress, and α and β are exponents, showing the elasticities of capital and labour with respect to output. α and β sum to 1 - implying that a one per cent increase in both capital and labour leads to a one per cent increase in output.

Meade's extension of the neo-classical approach results in a somewhat more sophisticated production function:

$$Y = f(K,L,R,t)$$

where K, L and R are capital stock, labour, and land respectively, and t represents technological change. Where only land is fixed, growth can be expressed as:

$$\frac{\Delta Y}{Y} = \frac{aK}{Y}\cdot\frac{\Delta K}{K} + \frac{bL}{Y}\cdot\frac{\Delta L}{L} + \frac{\Delta Y^{1}}{Y}$$

where $\Delta K/K$, $\Delta L/L$ and $\Delta Y^1/Y$ represent rates of increase of capital, labour, and technological progress, and aK/Y and bL/Y are the elasticities of output with respect to

试读结束，需要全本PDF请购买 www.ertongbook.com