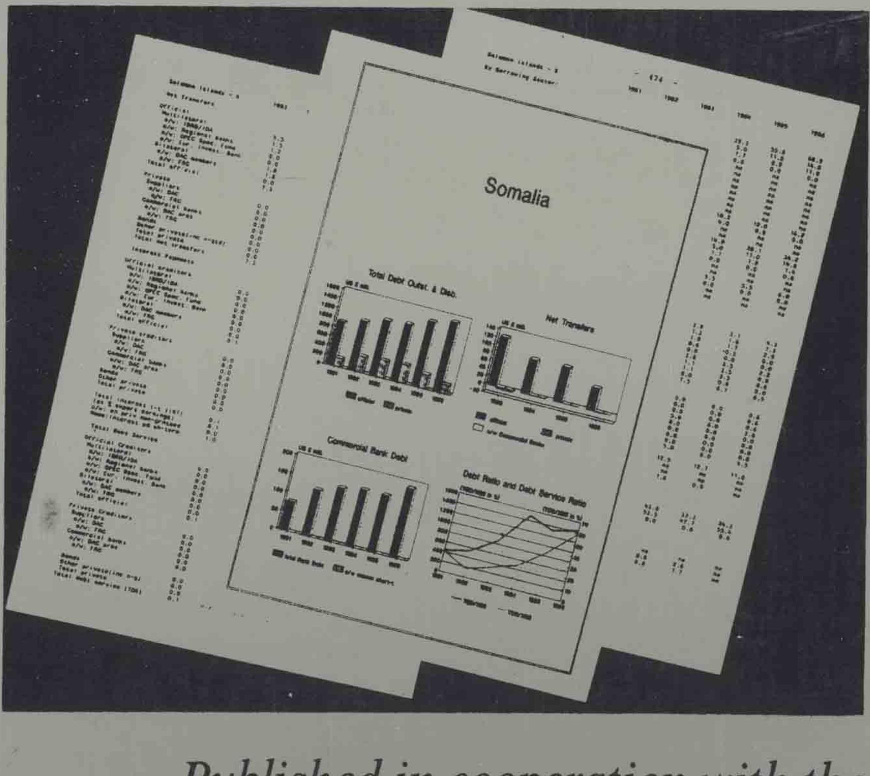
Dieter Strack
and Siegfried Schönherr
editors

Debt Survey of Developing Countries



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Debt Survey of Developing Countries

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The IFO Debt Survey was prepared between October 1986 and December 1988. The cut-off date was fixed as 31 December 1986 for all reporting systems included. All data were last revised in July 1988.

The concept of the IFO Debt Survey has been designed and operationalized by Dieter Strack. All programming and data compilation was done under the responsibility of John Gregory. Professional input has been provided by various experts and scientists. Anton Gälli and Rigmar Osterkamp made valuable contributions during the process of concept development. Siegfried Schönherr took up the task of overall coordination.

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Contents

1. Preface: Why Another Debt Survey?

Statistics on external debt of developing countries have, for a number of years, been compiled by various international organizations, notably by the International Bank for Reconstruction and Development (IBRD) - the World Bank-, the International Monetary Fund (IMF), the Organisation for Economic Co-operation and Development (OECD) and the Bank for International Settlements (BIS) which pioneered the compiling of international debt statistics. All of these organizations view the external debt issue with a different perspective, each institution having its own constraints and objectives. Consequently, they all apply different methodologies when compiling debt data on the external obligations of a given country. There are also significant differences in coverage, due to variations in the scope of their individual reporting systems.

In recent years, with yet another objective, commercial banks, especially those with significant lending portfolios to developing countries (DCs), have started to collect data on bank lending to these countries; an exercise which is directed through the bank-sponsored Institute for International Finance (IIF) in Washington, D.C..

Whereas the commercial banks do not generally publish country specific bank debt data of DCs, the international organizations mentioned above do periodically publish country related debt data aggregated from the information available in their individual reporting systems. Although, on rather specific issues like export credits, there is some exchange of information between these organizations, considerable differences both in the presentation of debt data and in values remain, caused by differences in definitions, approaches and compilation methods used by the organizations concerned. This, as mentioned already, is due to their differing practical needs for which the debt data was compiled in the first place.

There is not only a significant difference in geographical coverage between the organizations actively involved in collecting and publishing debt data, there is, even more importantly, hardly more than a minimum agreement on what constitutes debt (the so-called "core definition"). It is therefore inevitable that the values on external debt, both country related aggregates and the grand total, as published by the organizations differ, and at times considerably. This is due to the fact that none of the organizations could be said to be producing comprehensive information on external debt. Even when combining the information on developing countries' external obligations, a remarkable (though difficult to quantify) information gap remains, largely concerned with commercial bank loans to non-banks in developing countries and with liabilities of non-banks in borrowing countries to non-banks in creditor countries.

The Debt Survey compiled by the IFO Institute is, for the first time, combining in a coherent and comprehensive way, the maximum of external debt related information available at the World Bank, the IMF, the OECD and the BIS, supplemented by a considerable amount of information privately provided to the Institute by the international banking community. The Survey is geared to fill, to the extent possible, the prevailing information gap mentioned above; its presentation is aimed at facilitating the use of external debt data by country analysts and other users, both in research circles and government agencies.

Lack of reliable data on the debt situation of developing countries is a serious handicap which has been widely cited as one of the major difficulties facing the international credit markets in the 1980s. It was perhaps itself contributing to the debt crisis.

Generally, no questions are raised as concerns official credits and, to a lesser extent, public and publicly guaranteed loans. Official credits to developing countries are almost entirely recorded by the joint OECD/IBRD sponsored Creditor Reporting System (CRS), based on loan-by-loan information, whereas the IBRD's Debtor Reporting System (DRS), is based on loan-by-loan debtor information, and contains a rather comprehensive record of public or publicly guaranteed credits to those countries covered by the DRS. The system currently covers 109 countries, it is thus not a global reporting system, a fact that constitutes its main deficiency. For practical purposes, the geographical coverage of this Survey is identical to that of the DRS.

Reporting of private non-guaranteed loans is relatively weak under DRS; only some 24 countries report aggregate data on private non-guaranteed debt to IBRD. Detailed data are available only in countries that have registration requirements covering private debt, most commonly in connection with exchange controls. If such requirements are not in place, countries mostly rely on balance of payments data and on financial surveys.

With official and public or publicly guaranteed loans being relatively well recorded, gaps in the publicly available data still remain in the area of commercial loans; even where such data is available uncertainties exist over its quality. Since January 1984 information on commercial bank loans, which represents the core of this Survey's analysis, has been significantly improved by the new IMF International Banking Statistics (IBS), periodically published in the International Financial Statistics (IFS), which fills the gap in the BIS statistics as concerns DC banks' borrowing via certain offshore financial centres.

Even so, quite a number of borrowings of DC non-banks from international commercial banks are not fully recorded; DC non-bank borrowing from foreign non-banks completely escapes recording; as does intra-company lending and equity-type liabilities. Some reporting from international banking centres results in an understatement of the actual claims on a given country, since when a loan or security has become non-performing it is reduced or eliminated from the balance sheets of the banks concerned even though the claim on the debtor still exists.

It was one of the main objectives of this Survey to fill the gaps mentioned above to the extent possible by supplementing the publicly available data with information which was provided to IFO by the international banking community and other sources which have requested anonymity. Recording by the international banking community covers 43 developing countries which are said to represent the bulk of DC borrowing from commercial banks. With the additional information referred to above, the Survey aims at an almost complete picture of the external financing situation of those 109 developing countries which were subject to the analysis. A small information gap is, however, likely to remain since no reporting system will guarantee a one hundred percent coverage.

Although pursuing the objective of a complete picture, it is evident that in most cases the total external debt stock of a given country will show a different value to that expressed in any of the existing official debt statistics. In a number of cases, the country related total value of external debt published in this Survey is considerably higher than that to be found in the publications of the official financial institutions. At the Annual Meeting of the IMF and the World Bank in September 1988, the IFO welcomed the opportunity to discuss these issues with representatives of the major commercial banks who confirmed that the values indicated in the Survey for individual countries came very close to the current market estimate of those countries' external obligations.

The other aim of this multifaceted Survey, next to filling the information gap on a country's total external indebtedness, was to illustrate what forms of debt are involved and to demonstrate how a country's external debt is related to other economic indicators. For the first time in the "history" of external debt statistics, this Survey *inter alia*

- provides a computation of the individual countries' excess short-term debt which is regarded as a key factor in analysing the financial situation and creditworthiness of a developing country,

- shows the liquidity position of a country,

- deals with the country's external payment arrears,

- provides a complete breakdown of long-term loans by borrowing sector indicating the share of commercial banks, and

- shows creditor breakdowns not available in any other international debt statistics.

This Survey is thus not just another compendium of international debt statistics, but represents a conscious attempt to meet the requirements of country analysts who regard working with the official statistics on external debt of developing countries a tedious and time-consuming business, due to shortcomings in the data and to the different methodologies employed.

The authors would like to express their gratitude to a number of persons, organizations and banks for having so generously assisted in the compilation of this Survey. They are highly "indebted" to members of the staff of the International Finance Division of IBRD, to the Executive Director of the Federal Republic of Germany at the World Bank, to staff members of the International Banking Division of the IMF, to the Director and analysts of the Institute for International Finance in Washington D.C., to the senior economists of the Monetary and Economic Department of the BIS in Basle and to the OECD in Paris. Much helpful advice and assistance was provided by the staff of the Money, Finance and Development Division of the United Nations Conference on Trade and Development (UNCTAD) in Geneva. Finally, they thank the members of the Research Division of the American Express International Banking Corporation in London for their analytical input which was much appreciated.

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2. Remarks on the Debt Situation and Related Methodological Issues

The size of total external debt of developing countries continued to rise in 1985/86, from $1,333.1 million at the end of 1985 to around $1,417 million at year-end of 1986, a rise of 6.4% . Approximately $1,034 million of this debt is owed to private creditors, notably commercial banks; over $380 million is official debt, including credits from multilateral organizations. These figures also show that the external debt is significantly higher than that published by official sources.

The increase mentioned above was somewhat smaller than the nominal rise in Total External Debt registered the year before. It should be noted that the real increase was even smaller (in the order of 2 to 2.3%) as the bulk of the nominal increase was due to a sharp depreciation of the dollar against other major currencies, especially the Deutsche Mark (DM) and the Yen.

While looking at debt statistics, it should be kept in mind that the currency valuation effect plays a significant role in determining debt in real terms. The impact of exchange rate changes on any debt aggregate depends highly on its currency composition: the higher the dollar share, the lower the impact. An appreciation of the US currency results in an understating of reported increases in aggregate debt data being expressed in dollars, as the appreciation reduces the dollar value of the debt component denominated in currencies other than US dollar like DM, Yen, Swiss Franc etc. When the dollar depreciates, this exchange rate effect on debt aggregates is reversed. Thus, the aggregates in current dollars are biased downward in times of dollar appreciation and upward during times of dollar depreciation. Consequently, for certain areas the currency-adjusted growth of total debt was considerably lower than nominal growth: just 20% of nominal growth in Latin America, and even a decrease in real terms in East Asia and the Pacific. In these areas the dollar denominated loans are overwhelmingly dominating. Full information on the currency composition of loans is not available as this is regarded as being strictly confidential. However, one can reasonably assume that about 75% of total international bank credit to developing countries (DCs) is denominated in dollars. The share of dollar denominated loans for sub-Saharan Africa is about 45% . According to sources at the OECD, the share for all low-income countries is under 40% .

The effect of the change of dollar value is rather difficult to measure. In financial circles a simplified equation for measuring the impact on a given stock of a change in the dollar value is used:

$$D = \frac{r\,(x-100)}{(100+r)}$$

where,

D = percentage change of the sum expressed in dollars,
r = percentage increase in the exchange of the dollar against all other convertible currencies together, and
x = percentage share of the sum which is denominated in dollars at the beginning of the period.

It is assumed that when loans have a 60% dollar content, a change in the dollar value of +10 % results in an impact of -3.64 % on reported debt, whereas a change of -10% results in an impact of +4.44 % on reported debt stock.

Although the increase in the total amount of debt thus showed a tendency to slow down, the costs of servicing this debt remained high with a tendency to increase. According to the International Bank for Reconstruction and Development (IBRD), the total debt service on the long-term debt of the 109 countries covered by IBRD's Debtor Reporting System (DRS) amounted to just over $116 million in 1986 being equivalent to 26.7% of the exports of capital-importing countries. Interest payments alone amounted to 12.8% of total export earnings of this group of countries in 1986.

The debt situation of a large number of countries, however, is much more critical than the overall picture suggests. Developing countries can be classified into broad categories, according to the seriousness and type of their debt problem. Most seriously affected by the ongoing crisis, as reflected by their high debt-service ratios are notably:

- the 15 heavily indebted countries (HICs); these countries are included in the "Baker Proposal" which the former US Secretary of the Treasury pronounced in 1985. They rely mainly on commercial bank credit.

- the low-income countries, particularly those in the the sub-Saharan region. Although relying mainly on official credit, they are nonetheless severely hit by financial problems, given their low per capita income and the narrowness of their production base.

For both groups one can note from the outset that annual GDP growth during 1980-86 was extremely low, even being negative in some countries. This clearly shows that debt has become a major constraint on growth. The gloomy growth prospects will, in turn, weaken even more the future debt-servicing capacity of debtor countries.

Further, the serious decline in export earnings of developing countries, mainly due to the continued fall in commodity prices, has aggravated the situation. As the most commodity-dependent region in the world, sub-Saharan Africa has suffered a huge contraction in export revenues on account of the slump in commodity prices since the 1970s. The real price index for sub-Saharan Africa's 16 main non-oil commodities (obtained by deflating their nominal price index by the trend in manufactured import prices) peaked in 1977 and is now only half what it was then. If oil exports are included, the region's real export prices rose to a plateau in 1982-84 and then declined precipitously in 1986 to about half their 1982-84 level.

The United Nations Secretary-General's Advisory Group on Financial Flows to Africa which has recently released its report noted that African countries' terms of trade have deteriorated regardless of whether their exports have predominantly been agricultural commodities, non-fuel minerals or oil.

Indeed, as long as exports grew faster than interest payments, debt servicing did not pose any problem. However, for debtor developing countries, and especially for those most affected by the debt crisis, the growth ratio of exports during the period 1980-86 was far below the average interest rate, with the exception of 1984. Over most of these years the growth rate of exports was even negative.

Still, under the prevailing strategies to cope with the crisis, it is a requirement that developing countries finance debt service from trade surpluses rather than from additional capital inflows. The development of debt-service/export ratios of a large number of developing countries prove the inadequacy of the current international strategy to restore the problem.

The export surplus strategy is counter-productive in many ways: if import compression is the chosen route to achieve such surpluses, this undermines economic growth and reduces consumption in the countries concerned; it pushes countries further towards undesirable protectionist policies; and it affects the capital formation necessary for future creditworthiness. Due to these import restraints, imports into the countries of sub-Saharan Africa, for example, have been squeezed to the levels of 20 years ago. As a result, incomes have been reduced, development programmes disrupted, and basic social services have deteriorated. By cutting customs receipts, the decline in imports has curtailed public revenues and constrained public budgets, which had, in particular, serious effects on the health and education systems in the countries concerned.

The expansion of exports to achieve the goal relies, at a time of falling commodity prices, on large volumes, whereas export expansion in the manufacturing sector is likely to meet protectionist barriers to trade in export markets especially in the United States. An export surplus strategy as a means of solving the debt crisis may be applicable to a limited number of Latin American debtors; Brazil for example, is held out as a model in that respect. But the idea that poor countries are required to effectively transfer wealth to rich countries through trade surpluses is unacceptable in the long run.

The debt-service burden of the HICs remains very high. Although interest rates were declining in the past, which is important for this group of countries as they have accrued the bulk of their debt on commercial terms, the debt-service burden significantly increased in 1986, when their debt service costs amounted to 38% of their exports, more than half of this was accounted for by interest payments. Still, the major middle-income (Latin American) debtors that form the core of the HICs are in a relatively more comfortable position than for example the sub-Saharan countries, despite their overwhelming total amount of debt outstanding in absolute terms. For these countries, the debt problem is felt as a major liquidity crisis, mainly caused by adverse international economic conditions (high interest rates and slack growth in the industrialized countries) and by an excessive accumulation of commercial liabilities with undesirable characteristics (short maturities, flexible interest rates, etc.). But, generally, these major middle-income debtor countries should, in the long run, be in a position to use substantial amounts of external commercial finance to service their debt.

The situation of the low-income countries, i.e. mainly the sub-Saharan countries, is totally different from this and, at least potentially, much more dangerous.

Although their total debt stock is relatively small (under 10 % of the developing countries' total) their debt ratios are considerably worse. For sub-Saharan Africa as a whole, including Nigeria which is generally viewed as a special case because of its size and its status as a large oil exporter, actual debt service payments averaged $7.7 billion a year in 1984-86. Excluding Nigeria, the region paid $2.1 billion more per annum in interest than in 1979-81. But even this does not fully reflect the magnitude of the region's financial problems, since many countries have been unable to meet all their debt servicing obligations. Between $5 and $6 billion of debt service due in 1986 was not actually paid because of rescheduling agreements or the accumulation of arrears.

The situation in sub-Saharan countries developed to a point where these countries, in the jargon of World Bank economists became "debt-distressed". Nearly 90% of the debt-distressed countries owe their debt to governments or other official creditors.

This heavy debt burden and, in particular, the resulting interest arrears, have in the past effectively blocked new commitments and disbursements from all official sources, including multilateral development agencies and the IMF. Official flows on non-concessional terms have fallen drastically, mainly because of a sharp turnaround in IMF net lending. African countries now have to repay large credits made available by the International Monetary Fund earlier in the decade, with the results that there were net flows of well over $400 million from sub-Saharan Africa to the IMF in both 1986 and 1987 and net transfers of almost $900 million a year if interest charges to the Fund are included.

But it is not credit on non-concessional terms, it is concessional public finance which the low-income countries need most, as their high level of dependence on a narrow range of primary commodity exports with poor long-term prospects makes it extremely difficult, if not impossible, to ensure that debt on commercial or near-commercial terms is serviced.

Even relatively optimistic economic forecasts suggest that the situation of debt-laden low-income countries in Africa is likely to get worse. It is absolutely crucial for the reconstruction of conditions needed for growth that ample Official Development Assistance (ODA) is made available to this group of debt-distressed countries. UN economists have calculated that $1.5 billion in additional resources is required annually for 14 low income African countries (one quarter of sub-Saharan Africa's economy) just to secure 1 per cent per capita import growth and reduce their average debt service ratio to 25 per cent. Extrapolating on this figure, it is assumed that, for the sub-Saharan region as a whole, with the exception of Nigeria, over $5 billion per year would be required to meet import and debt service objectives[1]. As the President of the World Bank recently stated, the reforms in countries eligible (i.e. the low-income countries) for financial assistance from the International Development Association (IDA) with adjustment programmes "will fall far short of these objectives if major increases in medium-term public finance are not forthcoming"[2].

With the attention of the international community focusing on Latin American debtor countries, the urgency of the debt problems of low-income African debtor countries has only lately gained recognition. At the Venice Summit Meeting, the leaders of the most important industrialized nations recommended easing the debt-service terms of the poorest African nations that are undertaking adjustment efforts. These recommendations were again repeated at the summit meeting held in Toronto in June 1988; they were aimed at the Paris Club where official creditors negotiate longer-term reschedulings for developing countries. Subsequently, Mozambique and Somalia, have each been given twenty-year reschedulings with a 10-year grace period.

The International Monetary Fund (IMF) introduced the Enhanced Structural Adjustment Facility (ESAF) of SDR6 billion ($8.4 billion) with considerably softer terms than the normal Structural Adjustment Facility (SAF). With an interest rate subsidy financed by grants from donor countries, this will approximately triple the Fund's concessional resources for low-income countries.

Rescheduling of non-concessional bilateral claims, which represent more than 50% of total bilateral credit to sub-Saharan countries, is often difficult as the bulk of this credit is provided by official export credit agencies which cannot easily absorb the losses implicit in lower lending rates. However, during the last year, one has noted a certain growing flexibility on behalf of export credit agencies. Juxtaposed against this increased willingness of the agencies to provide new terms in the rescheduling process, there is a reported sharp decline in new business "responding to the more difficult international environment by cutting back sharply on public expenditure, in particular the very large projects for which official export credit support had typically been sought" as the IMF notes[3]. An increasing number of countries ran up arrears and were consequently disqualified for cover, and as a result their export credit virtually disappeared. Even recently, amortization repayments to export credit agencies remained very high, thus increasing steadily the gross to net ratio for medium and long-term export credit. Without departing substantially from past practice the IMF has now suggested a variety of ways in which export credit agencies could contribute more effectively to adjustment in low income countries[4].

The other debt aggregates developed as follows in 1986 (the latest year for which data are recorded):

- The private non-guaranteed debt stock declined, caused by net repayments over the year. This decline was partly due to the fact that private non-guaranteed liabilities were taken over by the governments through the rescheduling process thus turning private into public debt; on the other hand this decline was the result of negative loan flows, as principal repayments, especially in East Asia and in Latin America were higher than disbursements.

- Short-term debt, especially in East Asia and Latin America declined considerably.

- Public debt showed a sharp rise in 1986, partly reflecting the already mentioned take-over of private non-guaranteed debt by governments. In 1986, the share of public debt in total external liabilities of all developing countries reporting under the DRS continued to grow; in the heavily indebted countries this ratio almost doubled in the period from 1982 to 1986.

- Use of IMF credit denominated in SDRs increased only slightly, however, the International Monetary Fund recorded a net repayment which, as mentioned earlier, was rather significant in the case of sub-Saharan countries.

  It should be noted that multilateral debt (IMF and others) now represents a major burden for certain categories of DCs. In 1986, the multilateral agencies (including IMF) accounted for nearly 18% of the external debt of sub-Saharan countries and for about one third of the debt of the low-income debt-distressed countries in Africa. Honoring multilateral debt obligations in the present economic circumstances imposes severe constraints on both the balance of payments and the public budget of debtor countries. Note that such obligations are ineligible for rescheduling; failure to remain current entails loss of access to further finance and, in the case of arrears to the International Monetary Fund, to the possibility of rescheduling official debts at the Paris Club. The growth rate for Latin American debt remained virtually unchanged in 1986, whereas that for South Asian debt continued to grow.

- Total net flow of finance to the countries under consideration in this analysis again dropped sharply from $33.5 billion in 1985 to $25.0 billion at end-1986.

- Official financial flows to developing countries as a whole increased, but this increase was, however, largely due to the depreciation of the dollar against other major currencies. Using 1985-based dollars and prices, official financial flows actually declined. There was, however, some increase in real terms in net flow of official credits to sub-Saharan African countries as well as to the group of the least developed countries in 1986. Still, the situation in these countries remains highly critical and is under extensive international examination. The sharpest decline in net flows were registered on both Latin American and Eastern Asian countries.

- Interest payments again increased during the last year despite the fall in interest rates in world capital markets.

- As a result of declining net flows and rising interest payments the net transfer from developing countries to their creditors rose sharply from $22.3 billion at end-1985 to $30.5 billion at end-1986.

- Private flows from all sources to the countries analyzed declined from $54.1 billion in 1980 to $5.5 billion in 1986.

- The volume of commercial bank credit, the largest component of private flows, to developing countries (other than offshore banking centres) has declined drastically and by end-1986 it had almost completely dried up. The majority of DCs have, in the eyes of commercial banks, entirely lost creditworthiness.

During 1987, the current account position of developing countries as a whole improved rather markedly partly as a result of somewhat higher commodity prices during the past year.

The resulting increase in official foreign exchange reserves was partly deposited with BIS reporting banks where deposits from DCs increased by $18.5 billion during the first half of 1987, in contrast to a reduction of $18.3 billion during the first half of the preceding year. It should be noted, however, that the Taiwan Province of China accounted for most of these deposits ($11.9 billion) with Mexico having deposited $5.8 billion and the People's Republic of China $2.1 billion.

There was some resumption of commercial bank lending to DCs in the first half of 1987, whether voluntary or involuntary; developing countries (other than offshore centers) borrowed $3.4 billion from commercial banks, compared to almost zero in 1986. This increase in bank finance to DCs reflected a modest increase in commercial bank claims on developing countries of approximately $3 billion. Africa was the only region that failed to register net new commercial bank lending. Countries not experiencing debt-service problems raised $3.1 billion net, whereas lending to countries which do experience debt-service problems (the so-called problem debtors) only amounted to $0.3 billion.

During the first half of 1987, the "Baker countries" repaid $0.3 billion to banks, compared to a repayment of $1.9 billion in the first half of 1986. Generally, the share of bank claims on DCs continued to decline in 1987.

Debt converted in 1987 (first nine months) amounted to approximately $2.3 billion, compared to $1.6 billion in 1986. In addition, the sale of $0.8 billion in claims of Japanese creditors to a Japanese non-bank entity in the Cayman Islands as well as unrecorded sales by other banks to non-banks reduced reported bank claims on DCs accordingly.

Concerted lending (or "new money"), which refers to equiproportional increases in exposure co-ordinated by the Advisory Committee of the commercial banks involved, amounted in the first half of 1987 to $14.5 billion ($3.5 billion to Mexico minus the repayment of a $0.5 billion bridge loan disbursed in 1986 and $9 billion to Panama). This amount already more than equalled total concerted lending during 1986.

Gross international bond issues by borrowers in DCs continued the declining trend of 1986 and amounted to $1.9 billion in the first half of 1987. For the first time in many years, there were no international bond issues from borrowers in Africa (excluding the Republic of South Africa), mainly due to the fact that Algeria was, for the first time in many years, not issuing bonds.

In 1987, according to first estimates, developing countries registered a net outflow of bank credit of $15 billion, this amount, however, came largely from non-problem debtors through considerable repayments made ahead of schedule.

African, and, in particular, sub-Saharan DCs continued to show negative net transfers to commercial banks in 1987. Exposure of commercial banks to African countries slightly increased, which is partly due to an increase in the consolidated positions of UK banks. However, German banks seem to have reduced their claims on DCs in general and on African DCs in particular. US banks continued to reduce their consolidated claims on DCs, albeit at a decelerated pace compared to 1986.

The terms of new commercial bank lending to developing countries in 1987 continued to ease both in concerted and spontaneous lending. Spreads over LIBOR, generally, continued to decline and average maturity of new commitments was considerably expanded, partly due to larger maturities related to concerted lending. In the period 1986 to 1987, average maturity expanded by approximately 38% to 11 years and two months.

3. Current International Approaches to Debt Problem Management

The major approach of providing relief to countries which have run into financial difficulties has been the case-by-case rescheduling of debt either in the Paris Club, dealing with official debt, or in the so-called London Club, for commercial bank debt.

Rescheduling has become a more-or-less a routine feature; it is certainly the most prominent instrument in international debt management. However, in the absence of the provision of new money, debt reschedulings, though they gave debtor countries a breathing space, have made the debt burden heavier by contributing to the piling-up of the stock of outstanding debt.

Generally, reschedulings, both for private and official debt, have led to easier conditions of repayment in terms of longer maturities and, in the case of commercial bank reschedulings, of reduced spreads and commissions.

Official creditors in the Paris Club require two preconditions for the initiation of debt reschedulings. Firstly, they must be convinced that the debtor country will otherwise be unable to meet its external payment obligations; secondly, the country must engage in an exercise designed to achieve a durable solution under the guidance of the IMF. One should note that creditors only agree to hold a meeting after debt servicing problems have reached a critical stage. There is little attempt at preventive action. Furthermore, official creditors are only agreeable to debt rescheduling if the requesting country has in effect an IMF programme making it eligible for upper credit tranche drawings. These requirements, in fact, have become a major stumbling block in current creditor/debtor relations.

Normally, the Paris Club type reschedulings cover both principal and interest on medium-term and long-term credit. There is a strong tendency to carefully avoid the rescheduling of short-term loans, since, in the majority of cases, such exclusion permits the maintenance of crucial short-term trade credits. Each official debt rescheduling agreement contains a *de minimis* clause. Loans below the *de minimis* level (between $250 thousand and $1 million depending on the country) are excluded from being rescheduled.

While official debt rescheduling certainly provided some relief, the absence of rescheduling for more than one year's maturing principal required repeated renegotiations which proved to be an extremely complex and time-consuming business. Creditors have tried to overcome this shortfall by negotiating Multi-Year Rescheduling Agreements (MYRAs) providing next to administrative simplicity some medium-term frame for economic adjustment.

However, MYRAs, with the exception of the agreement reached with Congo, have in the past been concluded exclusively with middle-income debtor countries, while Africa, in particular the sub-Saharan part, was "treated on the short leash basis" as the Commonwealth Secretariat recently noted in a statement.

One additional step, already been taken by some bilateral donors, is to convert official development assistance loans into grants. The UN recommended that this be extended to all existing Official Development Assistance (ODA) claims on low-income, heavily-indebted African countries. However, it is realized that this would bring only modest additional resources, given the fact that these loans already carry low interest rates and relatively long grace periods for repayment of principal.

A measure which would be much more efficient would be the reduction of interest rates during Paris Club reschedulings on non-concessional debt. Here, some donor countries, especially the UK and the Nordic countries have been proposing to ceil these interest rates to an International Development Association (IDA) level. IDA loans are provided by the World Bank at no interest and a very small service charge.

In all, $390 billion of maturities have been rescheduled since 1980, $68 billion with official creditors and $321 billion with commercial banks, i.e. 470% more than within the framework of the Paris Club, which indicates the importance of rescheduling of commercial bank credit.

These commercial bank debt restructurings have the following main features:

- Normally, only debt principal is restructured, and arrears are expected to be repaid when the agreement goes into effect. Because of regulatory restrictions in a number of creditor countries, interest is not capitalized but refinanced by the provision of new loans (in proportion to existing exposure). Banks may maintain or extend short-term credit facilities.

- As with official reschedulings, private creditors also ask for a stand-by agreement with the IMF as a precondition for restructuring, although commercial banks have been somewhat less rigid in this respect, especially while concluding MYRAs.

- In most recent bank rescheduling agreements, a range of options have been included, so as to allow commercial banks to transform their claims in a way that best suit their business interests in a particular country.

The "menu of options", an approach explicitly encouraged by creditor governments[5], includes currency redenomination, conversion of debt to equity and other newly-developed techniques.

The option of "exit bonds" as agreed in the case of the 1987 Argentine rescheduling provides the possibility to commercial banks with relatively small exposures subscribing to such bonds to stop taking part in further loans and reschedulings. Exit bonds carry low interest.

New money bonds were another option to attract banks to participate in new money packages. New money bonds are viewed by many banks as more attractive than participating in a syndicated loan as the vehicle for new money, as bonds have some characteristics of a senior claim on the issuing country.

Within this framework, the new terms agreed upon by banks in recent commercial bank debt restructuring agreements have been noticeably improved, thus continuing the trend over the past three years to extend maturities and grace periods for all debtor countries (in 1987 average maturity was up to fifteen years from ten years in 1986). Spreads over LIBOR have been significantly reduced to about 1 % in 1987, which is about half the value of the previous year.

However, the amount of new money has continuously declined as it became increasingly difficult to reach agreement between debtor country authorities and bank advisory committees on both the scale and terms of further concerted financing.

In several cases, the World Bank has been asked by the commercial banks concerned to provide co-financing as has been the IMF. The Fund, however, in order to put more pressure on commercial banks, has repeatedly informed participating financial institutions that arrangements to use its resources would not enter into effect until assurances have been received from a "critical mass" of bank creditors (i.e. banks accounting for about 90% of the proposed new money package). The IMF repeatedly argued that commercial banks had a strong collective interest in providing liquidity.

The reluctance of commercial banks to provide new money has been further reinforced by the move taken last year by major US banks to substantially increase their loan loss reserves in respect to their loans to developing countries (Citicorp $3 billion, Chase Manhattan $1.6 billion, Hanovers Manufacturers $1.7 billion, etc.).

This undoubtedly reflected the re-evaluation of commercial banks of their lending portfolios in time with the high discounts on developing country debts in secondary markets. According to Salomon Brothers in New York the (bid) price for Argentine loans dropped from 64¢ (per $ of loan face value) in June 1983 to 37¢ in September 1987. Nigerian loans were valuated 55¢ and 25¢ respectively.

The discount on developing country debt can also be utilized in order to reduce individual countries' liabilities to levels more compatible with resumed growth.

Bolivia, for example, bought part of her external obligations back, at heavy discounts, for cancellation as concluded in an agreement with 131 commercial banks. The scheme will be monitored by the IMF where an account has been established. This account will be filled by donations made by donor countries and specially designated for the buy-back.

However, banks, in general, are against this practice of buy-back of a portion of debt by debtor countries, since this involves advance repayment to some creditors, thus breaking the clause of equal treatment of all creditors.

There are other options to reduce the debt burden of developing countries: Debt-to-equity swaps; debt-for-goods swaps (another form of countertrade); and conversion of external debt into local currency for use by charitable organizations.

Among the debt conversion schemes mentioned above, the mechanism of debt-to-equity swaps has received the most attention in the past. Debt equity conversions so far account only for a small fraction of debt outstanding; they are certainly not the solution to the debt crisis of developing countries, hence, where applicable, they offer a way of reducing the foreign exchange needs to service the debt load, to encourage foreign investment and, nevertheless, offer a channel for the return of flight capital which bred large increases in debt. But, as Graham Bird rightly points out[6], there could well be consequental effects on the exchange rate, the domestic money supply and inflation. The local currency required for the purchase of external debt has to be provided by the monetary authorities of the debtor country, through either money creation or the issuance of domestic public debt. Excessive money growth or upward pressure on interest rates then may result.

By mid-1987 as Morgan Guarantee Trust in New York reports[7], eleven developing countries with a total of $267 billion bank debt had swapped external debt to equity resulting in the (modest) reduction of their debt burden by $6 billion or 2.2% of their total debt.

The debt conversion programme of Chile has been the most successful. This country converted approximately 14% of its total debt to foreign banks into equity. Other countries show a certain reluctance to go ahead. In 1987, the Group of Thirty issued an informal paper[8], on debt-to-equity swaps which was, on balance, critical because of a number of issues potentially attached to the implementation of the conversion schemes which, however, cannot be elaborated here further. Nigeria and Ecuador are presently thinking of setting up new programmes, while Costa Rica and Jamaica have just announced their programmes.

In particular, multinational corporations have, in the past, bought foreign debt of DCs and swapped them into equity, finding these swaps a relatively cheap way of raising and investing new capital in developing countries, especially Latin America. These corporations included Fiat, Eastman and General Electric. The question, however, is whether the schemes do not offer, in effect, a subsidy to foreign investment that would have taken place anyway.

The preparedness of a country to effectively implement a conversion scheme would, however, undoubtedly be understood as a signal to the international business community that the country will follow a liberalized investment policy in its drive to regain access to the international capital markets.

A number of funds are actually in existence to which subscribers contribute DC paper as David Roberts from the Federal Reserve Board in New York noted in an interview. The fund manager negotiates the terms of conversion with the DC government and builds up an equity portfolio. For the Philippines, New York-based Shearson Lehmann Brothers is currently putting together the First Philippines Capital Fund, with 80% of the planned $250 million coming from debt contribution.

The International Finance Corporation (IFC) in Washington, D.C. has similar plans, perhaps with political and transfer risk insurance from the Multilateral Investment Guarantee Agency (MIGA).

All these schemes are relatively new, they have to be evaluated as a function of the degree of actual debt relief they can provide and the possibilities for debtor countries to share the debt discount with new investors who have benefitted from transactions on the secondary markets.

Another approach would be the conversion of external debt into long term securities, which would carry a low rate of interest but could be assured of their value and liquidity. A proposal along these lines, involving the conversion of debt into securities of at least 20 years, has recently been floated by the African Development Bank. Under the scheme, designed by the British merchant bank S.G. Warburg and Company, all of an African government's bilateral and non-concessional debt (excluding IBRD and IMF loans) would be converted into long-term securities which would have the same face value as the debt for which they were exchanged. They would mature in at least 20 years, whereupon they would be repaid in full. Bearing a fixed rate of interest, they could be freely traded on the international capital markets. The long-term securities would be issued by an intermediary agency funded by and/or backed by the guarantees of major creditor governments against which commercial banks would exchange at a discount the DC loans in their portfolio. Consequently, the intermediary would replace the liabilities of debtor countries to banks by liabilities to itself. Thus, by assuming the risk of non-payment by debtors, creditor governments would be able both to improve the quality of bank assets, thereby strengthening the banking system, and to restore the debt overhang to DCs, thereby stimulating the growth of development[9].

Since the African Development Bank's President, Mr. Babacar Ndiaye, first unveiled the scheme at the Organisation of African Unity (OAU) Special Meeting on Africa's debt crisis in November 1987, some 15 African countries have been contacting the Bank about the possibility of applying the plan to their debts. It is reported from Abidjan that the Bank's discussions on the subject matter are furthest advanced with Zaire.

The other way of overcoming the shortcomings of the present approach to the debt crisis is for creditors to simply regard debt relief as a positive sum game and reduce their claims accordingly.

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1 External Debt Crisis and Development, The international debt situation in mid-1987, Report of the Secretary-General, United Nations, General Assembly, 42nd session, September 1987

2 Address of Mr. Barber B. Conable, President, The World Bank, to the Keidanren (Federation of Economic Organizations), Tokyo, 27.3.1988

3 Officially Supported Export Credits, Development and Prospects, World Economic and Financial Surveys, IMF, Washington, D.C., 1988, p.5

4 ibidem

5 The heads of State or Government of the seven major industrialized countries stated in their economic declaration of 10 June 1987 in Venice that "... we support efforts by commercial banks and debtor countries to develop a 'menu' of alternative negotiating procedures and financing techniques for providing continuing support to debtor countries".

6 Graham Bird, Debt Conversion and Capitalization in Principle and Practice (mimeograph), October 1986

7 World Financial Markets, Morgan Guaranty Trust Company of New York, June/July 1987, p.11

8 Group of Thirty, Debt-Equity Swaps, Informal Discussion Paper, New York, 1987

9 The first proposals of this kind were advanced in 1983 by Felix Rohatyn and Peter Kenen in: The Debt Crisis and the World Economy, Report by the Commonwealth Group of Experts (London: Commonwealth Secretariat, 1984). Similar approaches regarding relief through portfolio adjustments are presented in: W. R. Cline, Mobilizing Bank Lending to Developing Countries, Policy Analyses in International Economics, No.18 (Washington, D.C., Institute for International Economics, June 1987). A good summary of the newly proposed schemes is also provided by: UNCTAD, Trade and Development Report 1988, Geneva, September 1988

4. Definitions of Financial Aggregates

It should be noted that the term "debt" in this analysis implies a liability, represented by a financial instrument or other formal equivalent. A financial instrument, as defined by the United Nations System of National Accounts (SNA), is the existence of a contractual creditor/debtor relationship, excluding however, transfers involving gold and, by convention, Special Drawing Rights (SDRs). External debt is the amount, at any given time, of disbursed and outstanding contractual liabilities of residents of a country to non-residents to repay principal, with or without interest, or to pay interest, with or without principal.

Current Account Balance

Please note that the elements of Current Account as shown here do not always add up to the Balance, which includes Official Unrequited Transfers, if applicable. These transfers, generally very small, were omitted from the presentation.

Exchange rate

The number of units of local currency per SDR at the end of the reporting period.

International Interest Rate

This is the London Interbank Offer Rate (LIBOR) for six month dollar deposits as shown for the period in "International Financial Statistics" (IFS) plus 1.625% to allow for margin between bid and offer rates (0.125%) and spread (1.5 %). Concerning the spread figure used in the analysis, it is understood that there is a variation between countries' spreads; these figures, however, are not accurately recorded. Fine-tuning the analysis by taking this into account would be unlikely to make any significant difference to the conclusions to be drawn.

Official international reserves (excluding gold)

This entry denominates the total of a country's holdings of SDRs, its reserve position in the International Monetary Fund and its holdings of foreign exchange. SDRs and the reserve position in the Fund are unconditional Fund-related reserve assets. Foreign exchange includes monetary authorities' claims on foreigners in the form of bank deposits, treasury bills, short-term and long-term government securities and other claims usable in the event of a balance of payments deficit.

Official international reserves % imports (MGS)

The ratio of official international reserves to the total value of imports of goods, services and income payments.

Reserves/import coverage (months)

This is the ratio of official international reserves to the total value of imports of goods and services, expressed in months of coverage.

Official gold reserves

The value of official gold holdings, valued according to national practice, converted to US dollars.

Official gold reserves (thousand ounces)

This is the volume of official gold holdings in physical terms (thousands of fine troy ounces).