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THE DEVELOPING COUNTRY DEBT

In this issue

NOT HIGH ON COMMISSION'S AGENDA

The financial crisis threatens a new debt crisis in many developing countries. However, this issue is not high on the EU's agenda, the European Network on Debt and Development (Eurodad) says.

This is indicated by the outcome of the development ministers' meeting at the EU's General Affairs and External Relations Council on May 18. On the table was the annual communication package assessing European governments' progress in implementing their financing for development pledges.

The Communication consists of an overview paper titled 'supporting developing countries in coping with the crisis' and four European Commission staff working papers on Financing for Development (FfD), Aid for Trade, Aid Effectiveness and the MDGs.

The analysis and recommendations are primarily based on a questionnaire that the Commission's DG Development sends each year to EU Member States.

Eurodad regrets that the Council's conclusions dedicate one single paragraph to the debt issue that might soon become critical in a world financial crisis – and that paragraph contains no news.

The Council states that involvement of all creditors in international debt resolution mechanisms is necessary to ensure debt sustainability of low-income countries.

It pledges to continue supporting the existing debt relief initiatives, and "supports discussions, if relevant, on enhanced forms of sovereign debt restructuring mechanisms, based on existing frameworks and principles, including the Paris Club, with a broad creditors' and debtors participation and ensuring comparable burden-sharing among creditors with a central role for the Bretton Woods Institutions (BWI) in the debate".

According to Eurodad, the EC staff working papers are "a useful, if limited, accountability exercise" particularly as these show that much more needs to be done to implement existing European commitments on development finance, and to go further now that the financial and economic crisis is severely affecting developing countries and may push a further 100 million people into poverty in 2009."

The document acknowledges that since 2007, many post-Heavily Indebted Poor Countries (HIPC) have been particularly exposed to a succession of shocks – high and volatile food and energy prices – that have led them into new borrowing.

Eurodad says, even though the overview paper recognizes that due to the financial and economic crisis "developing countries will face a financing gap of $270 to $700 billion this year", the Commission's FfD paper does not recommend sufficient counter-measures.

Debt sustainability in developing countries is a major concern for the EU, but Member States' preference is to enhance existing debt management mechanisms, says Eurodad. However, only a minority of Member States acknowledges the need for a sovereign debt restructuring mechanism – they are thus showing little commitment to implement the Doha Declaration on FfD in this regard, says Eurodad. ☑

Voices of the South on Globalization is a monthly newsletter intended to inspire a meaningful North-South Dialogue by raising awareness for global interdependences and by offering a forum for voices from the South in the globalization debate. Each edition will present short analyses or commentaries from a Southern perspective on one particular issue of the globalization process.
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For further information please contact:
IPS-Inter Press Service Europe,
Ramesh Jaura, Marienstr. 19/20, 10117 Berlin
Tel.: ++49-(0)30-28 48 23 60
Fax: ++49-(0)30-28 48 2369
rjaura@ipseuropa.org

CONFERENCE REPORT:

ENDING SCOURGE OF DEBT

International debt campaigners are calling for the establishment of a debt arbitration mechanism to respond to the difficulties that many countries of the South are increasingly facing as they attempt to service debt arrears to international lenders.

Campaigners met in Johannesburg, South Africa, at a two-day international conference on a 'Fair and Transparent Arbitration Mechanism on Illegitimate and Odious Debts'. They oppose the status quo as one in which countries of the South are pushed further into debt.

They argue that the power wielded by the international financial institutions (IFIs) needs a rethink to protect the poor from the economic ravages that come with debt repayments. The campaigners suggested the establishment of a debt arbitration process to balance the interests of both creditors and debtors, particularly in the current global financial crisis.

''There is need for an approach that can deliver a durable solution to the debt crisis, acknowledging that debtors and creditors must share the responsibility for preventing and resolving unsustainable debt situations,'' according to Cephas Lumina, a United Nations' independent expert on the effects of foreign debt and related international financial obligations of states on the full enjoyment of rights.

Speaking in his personal capacity at the conference, he added that it was important to come up with a new debt solving mechanism outside the existing Paris and London Club framework. ''There is a lack of fair and transparent global governance, manifested in the dominance of creditors with regard to decision-making on resolving the debt crisis and the lack of debtor protection,'' argued Lumina.

BRUTAL IN NATURE

Opa Kampijimpanga, African Forum and Network on Debt and Development (AFRODAD) chairperson, said the current debt repayment mechanisms are brutal in nature and must be changed.

AFRODAD organised the conference, which ended Mar 31, in conjunction with the Economic Justice Network (EJN) of the Fellowship of Christian Councils in Southern Africa (FOCCISA).

AFRODAD is an organisation born out of the desire to secure lasting solutions to Africa's mounting debt problem which has impacted negatively on the continent's development processes. EJN is a non-profit southern African organisation.

''The current debt process is driven by a system which is brutal and capitalist in nature. We are calling for equal responsibility on debtor and creditor in view of corruption and the wrong policy advice given. The creditors must understand that they also make mistakes and should pay for their mistakes and not lay the full responsibility on debtor countries.'' He added that there was need to put in place a mechanism to protect countries of the South from some of the policy prescriptions put forward by the IFIs (the World Bank and the International Monetary Fund).

''There must be an arbitration mechanism formulated through the United Nations (UN) to give ordinary people who are suffering a voice to fight for their rights because their governments have proved to incapable of doing this,'' demanded Kampijimpanga.

But who will play that role if governments are too weak to do so? ''Civil society organisations can do it on behalf of citizens and present cases at the UN in line with the UN Charter which protects the rights of citizens,'' suggested Kampijimpanga. ''All we want is space to do so and a voice to say it.''

He lamented the poor responses of the international creditors to the problem of debt repayment in Africa, citing the Heavily Indebted Poor Countries (HIPC) initiative and the Multilateral Debt Relief Initiative (MDRI) as case studies.

HIPC was first launched in 1996 by the IMF and the World Bank. It was revised in 1999, linking debt relief to poverty reduction, macroeconomic stability and structural reform.

In order to qualify for debt relief under HIPC, a country must have an unsustainable debt burden, establish a track record of reforms and policies through World Bank and IMF-supported programmes and prepare a poverty reduction strategy paper (PRSP) through a broad-based participatory process.

MDG TARGET

PRSPs are the successor policy plans to the notorious structural adjustment programmes (SAPs) started in the 1980s. This is apparently aimed at reducing the amount of money paid by countries as debt repayments to international lending institutions. But the reality on the ground shows the contrary.

Several studies show that some countries are still spending more each year on servicing debt than they do on national programmes aimed at reducing poverty and improving a variety of social conditions, including health care, education nutrition and life expectancy.In its 2008 report, the Millennium Development Goals (MDG) Gap Task Force found out that the MDG target of dealing comprehensively with the debt problems of developing countries has not been achieved.

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CAMPAIGNERS WARN OF NEW 'GLOBAL DEBT CRISIS'

A new Jubilee Debt Campaign report has warned that a debt crisis approaching that of the 1980s could engulf many countries as a result of global financial turbulence. In the same week that UK Prime Minister Gordon Brown announced a World Bank fund for vulnerable countries, the new report said that at least 38 of world's most vulnerable countries risk spiralling debts due to financial crisis. It proposes alternative methods of helping those countries deal with the financial crisis without increasing long-term debt.

On March 9 Gordon Brown announced the UK would contribute $250million towards a new World Bank vulnerability fund which they hope will raise $5-6 billion altogether to spend on countries suffering for the financial crisis over the next 3-4 years.

Campaigners are concerned that the amount is too small, that it will be conditional on economic reforms and that a significant proportion is likely to take the form of non-concessional loans.

In the report, *'A New Debt Crisis?'* , published March 14, Jubilee Debt Campaign (JDC) warns that the significant falls in income and falling currencies expected in 2009 will seriously damage developing countries' ability to service and refinance their debts.

The 'Third World Debt Crisis' refers to the accumulation of debts, rapidly rising interest rates and falling commodity prices, which led many developing countries close to defaulting on their debts in the 1980s. Many countries spent huge sums of their budgets on debt servicing throughout the 1980s and 1990s, and some still spend more on debt servicing then on health, education and social services.

Of the 43 countries which the World Bank judges to be most vulnerable to the financial crisis, 38 had what we judged to be 'unpayable debts' before the crisis. (See World Bank statistics from The Global Economic Crisis: Assessing Vulnerability with a Poverty Lens, World Bank, 2009. Debt relief calculation based on research by new economics foundation, 2008.)

JDC believes that at least $270billion needs to be cancelled to allow those countries to fight poverty.

In particular:

- Zambia, which has already received debt cancellation once, could see its debts become twice the level deemed sustainable by the World Bank and IMF;
- The Philippines has $8 billion of debts that come up for repayment this year – something they may find impossible if the credit squeeze continues;
- Bangladesh, which is dependent on income from exporting garments to Europe and North America, is likely to suffer a major fall in demand which could make its debts unsustainable even by World Bank criteria.

The report lays the blame for the crisis at the failure to make radical changes to the international financial system after the first Debt Crisis and calls for these changes to be made immediately.

It demands a new wave of debt cancellation, led by an international 'Debt Tribunal', internationally binding responsible lending standards, and reform of the global tax system to allow developing countries greater independence from global finance.

A 'debt tribunal' is a proposed arbitration mechanism, at an international level, which could resolve sovereign debt crises and disputes in an open, impartial and transparent way, looking into debt legitimacy as well as the 'payability' of debts.

WAKEUP CALL

Sarah Edwards from Jubilee Debt Campaign said: "This is a wake up call to anyone who believes that the 'Third World Debt Crisis' has been solved. "The failure of the West to learn the lessons of that crisis, which in many ways mirrors the financial crisis the whole world is now experiencing, means that many countries are still suffering from debts arising from reckless lending 30 years ago.

"The funds which the Prime Minister announced . . . could make matters worse – they are likely to include new loans, with harmful conditions attached, when we should actually be cancelling old debts, without those conditions. We need a radically new international lending system, if we are to come out of the current financial crisis sooner rather than later."

Jubilee Debt Campaign is part of a global movement working for full cancellation of unjust and unpayable poor county debts by fair and transparent means. It is a UK coalition of around 90 national organisations and 100 local and regional groups, as well as thousands of individuals.

The report pleads for:

- Wider, deeper debt cancellation, amounting to at least $400 billion – a fraction of the bail-outs and stimulus packages recently proposed in the West;
- Radical reform of the World Bank and International Monetary Fund including removal of economic policy conditions from lending and debt relief, allowing countries to make their own policy choices, and full democratisation;
- Internationally agreed responsible lending standards which would bind governments, multilateral institutions and private lenders; and
- Efforts to assist developing countries in raising more domestic finance, for example by tackling illicit capital flight, so they are less dependent the debt cycle in the long-term. ☑

HIPC INITATIVE:

WOEFULLY INADEQUATE

The HIPC Initiative is viewed as a comprehensive approach to debt reduction for heavily indebted poor countries pursuing IMF- and World Bank-supported adjustment and reform programmes. But debt campaigners say the programme is woefully inadequate.

Although it was reformed in 1999, after G8 countries came under pressure from campaigners, it is still failing the world's poor, activists say. "It is time to abandon HIPC, and ensure that there is 100% cancellation of all unjust and unpayable debts, without harmful conditions."

The reasons:
1. HIPC is monitored and implemented by the World Bank and IMF. But most other creditors - rich countries, regional development banks and some private creditors - are encouraged to take part. Most, but not all, do. Commercial creditors in particular often fail to deliver their share of debt cancellation under HIPC.

2. HIPC is open to poor countries (generally, those with annual income per head of $935 or less), that have debts that are more than one and a half times their annual export earnings (or, if they have lots of exports, more than two and a half times their government revenue), and that have a World Bank and IMF programme. In order to embark on the HIPC scheme, they have to have a "track record" with the IMF: that is, have done what the IMF says for at least three years! Then they have to comply with a large number of conditions in order to complete HIPC and get debts cancelled.

3) HIPC was heralded by rich governments as offering "an exit from unsustainable debt". What this meant was a reduction in debt to a level deemed 'sustainable' by the World Bank and IMF. That level - regardless of a country's circumstances - was set as debt of one and a half times the value of export earnings.

On entering HIPC, countries get some relief on debt payments, and on completing HIPC (which can take many years), they get cancellation of debt to this 'sustainable' level. In 2005, thanks to an unprecedented level of campaigning on debt, this was extended.

Under the 'Multilateral Debt Relief Initiative' (MDRI), countries that complete HIPC now get cancellation of most debts to the IMF, African Development Fund and the World Bank. This is good news - but does not address the problems of HIPC conditions and structure, or the countries - and debts - left out.

4) When countries enter HIPC, a 'Decision Point document' sets out what they need to do to complete HIPC. Typically, these conditions will include measures to target poverty - but it also includes compliance with all kinds of economic policy conditions which can undermine poverty-reduction efforts.

For instance, countries have to cut public spending, meaning fewer teachers or doctors; they are told to privatise basic services like water or electricity, meaning worse service and higher prices for the poor; or they are made to liberalise trade, leaving poor farmers and producers unable to compete with imports from the rich world. Jubilee Debt Campaign's Cut the Strings campaign calls for an end to these conditions.

WHICH COUNTRIES HAVE COMPLETED HIPC?

Only 24 countries so far. These countries are: Benin, Bolivia, Burkina Faso, Burundi, Cameroon, Ethiopia, Gambia, Ghana, Guyana, Honduras, Madagascar, Malawi, Mali, Mauritania, Mozambique, Nicaragua, Niger, Rwanda, São Tomé and Príncipe, Senegal, Sierra Leone, Tanzania, Uganda and Zambia.

WHICH COUNTRIES HAVE ENTERED BUT NOT COMPLETED THE HIPC PROCESS?

A further ten countries have reached the first stage ('Decision Point') of the HIPC process, at which point they receive some relief on debt repayments. These countries are: Afghanistan, Central African Republic, Chad, Democratic Republic of Congo (Congo Kinshasa), Republic of Congo (Congo Brazzaville), Guinea, Guinea Bissau, Haiti and Liberia. Togo is the latest entrant to this group.

WHICH OTHER COUNTRIES ARE LIKELY TO ENTER HIPC?

Another six countries are eligible to enter the scheme: Comoros, Cote D'Ivoire, Eritrea, Nepal, Somalia and Sudan. However, they will first have to start programmes with the World Bank and IMF, and stay 'on track' with the IMF for three years. Other countries - like Kenya, Ecuador or Jamaica - are not considered poor or 'indebted' enough, by a calculation that takes no account of a country's human development needs or the origins of its debts.

SO, WHAT IS WRONG WITH HIPC?

- HIPC takes too long: more than 10 years for 24 countries so far.
- HIPC offers far too little - total cancellation of all unpayable and unjust debt is needed.
- HIPC is too limited - many more countries need and deserve debt cancellation.
- HIPC comes with damaging and unfair strings attached.
- HIPC does not include all debts: debts are only partially cancelled, and some countries, banks and companies refuse or fail to take part in the HIPC process at all.
- HIPC is entirely controlled by creditors: they do not accept responsibility for their part in creating and maintaining the debt crisis, or allow poor countries to have a say.

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DAC ACTION PLAN SKIPS DEBT ISSUE

Members of Development Assistance Committee, the world's major donor countries, and other donors, have adopted an Action Plan to support poor countries trying to cope with the economic and financial crisis. The Plan agreed at a high level meeting in Paris on May 27-28 will feed into several major international forums, such as the G8 Summit and UN Conference on the World Financial and Economic Crisis. However, the plan remains quiet on the developing country debt.

The participants took note that globally aid has risen and most donors are so far holding to their promises in the face of the crisis. ODA reached record levels in 2008, and is now some 80% of the projected 2010 level implied by our current commitments. In fact, they welcomed the announcement by the Obama administration of its proposal to double its ODA over the next five years.

But they also referred to the fact that despite this trend, some DAC members have decreased their aid and others are unlikely to meet their commitments. "The shortfall remains significant and aid to Africa is falling well behind pledges."

The participants took note that global downturn is affecting developing countries that are the least responsible for the crisis, and the least able to cope with its impact. Low-income countries, in particular, were already weakened by the food and energy crises.

A DAC press release says: The stakes are now high: The World Bank estimates that, as a result of the crisis, 53 million more people will have to live on less than $1.25 a day. In this context, the statement quotes Eckhard Deutscher, Chair of the Development Assistance Committee, saying: "We must not allow the current crisis to push millions of people back into poverty, reversing the progress for which developing countries have worked so hard."

The Action Plan says: "We all recognise the need for further collective momentum. We also recognise the risk of pressures towards additional aid tying as a result of the crisis.

- We reaffirm our existing ODA commitments, especially for Africa.
- In the spirit of the Accra Agenda for Action, we will resist pressures to tie aid.
- We will work within our governments for coherent use of all policy levers for development."

The action plan adds: "A return by 2011 to 2007 development levels still means four years lost on the road to the 2015 MDG horizon. For some low-income countries, recovery will be delayed further. Partner countries already face difficult tradeoffs between enduring priorities and urgent needs."

But thinking positive the action plan says: "The crisis also presents them (developing countries) with opportunities to reshape their strategies in a changing world economy. Aid provides a bridge to help countries safeguard social progress and social investments and at the same time build foundations for stronger, cleaner and fairer growth and the MDGs. Programmes in support of private sector development, employment and social protection, agriculture and food security, and infrastructure are central to this transition."

The plan adds: "Investing in women is critical at this time so that both women and men have the resources not only to survive - but also to thrive. Protecting developing countries from capital flight associated with tax evasion and strengthening asset recovery process are also action frontiers."

Against this backdrop, the DAC members pledge: "We will enhance our support for partner country priorities which help manage the impact of the crisis and underpin long-term development strategies, strengthened by accelerated action on gender equality. We believe aid can be catalytic in joining these two objectives."

They further pledge: "We will ensure that key commitments of the Paris Declaration and Accra Agenda for Action on country ownership, use of country systems and predictability are integral to the crisis response.

"We will signal clearly that any crisis responses, whether formulated at the country or at the international level, must be supportive of national strategies and processes. International coordination is not a substitute for country ownership.

"We will keep under review the thematic facilities developed in the crisis response context, and phase them out as appropriate, so as not to distort long-term recovery nor fragment the global architecture."

The Action Plan adds:
"We confirm our willingness to consider the potential need to deploy additional resources for multilateral institutions to help meet emerging needs at the country level.
"We recognise the value of multilateral crisis-response facilities and that voluntary bilateral contributions to them can be effective. These should be additional to resources at country level and not reduce predictability."

The DAC members also pledge to "strengthen monitoring and benchmarking of this landscape of activities financed by, and beyond, ODA and seek overall debt sustainability for partner countries" and to "promote complementarity between, and greater public understanding of, ODA and other forms of development finance."
The will also "coordinate around common country specific responses based on each partner country's plan and we will jointly and regularly monitor the impact of our support" and "regularly review the speed and coherence of the overall crisis response and hold ourselves to account for delivering the commitments we have made today, at next year's HLM and in following years. ☑

ENDING SCOURGE OF DEBT

(Continued fro page 2)

Despite the HIPC and MDRI debt relief and corresponding increases in social expenditures, a large number of developing countries still spend more on debt servicing than on public education or health. ''These were just blueprints from the IMF and World Bank with no input from African countries. It was supposed to provide a way out of debt but it achieved the opposite,'' argued Kampijimpanga. ''It is this one-size-fits-all mechanism that we want changed.''

Other speakers said the current debt repayment mechanism identifies the debtor countries as villains and put more emphasis on repayment than on realising the needs of the citizens, human rights and MDGs.

An example was given of the IMF's insistence that Zimbabwe must repay a loan of millions of dollars in debt arrears before it can release more loans. This is despite the fact that the new Zimbabwe government is struggling to provide basic services such as health care, clean water and education.

HIGH TIME FOR FAT MECHANISM

''It's a ridiculous demand by the IMF which should not be taken seriously'' declared Lumina Vitalis Meja from AFRODAD. He said it is high time a fair and transparent arbitration mechanism was put in place. ''We must make use of the UN to champion for stronger initiatives and tackle the financial institutions.''

But debt campaigner Charles Abraham believes there must be a consensus between the debtor and the creditor before such a mechanism can be established.

''You can only have arbitration by consent. There is no point in having it if there is no consensus. Both parties must agree, elect a forum and agree on composition of arbitration board members, decide on rules to be applicable and how the arbitration will play out,'' proposed Abrahams.

Lumina wants the arbitration body to be under the aegis of the UN: ''The establishment of an inclusive and equitable international debt arbitration mechanism must be under UN, which is the only international body with sufficient legitimacy to take a leading role in efforts to create an acceptable debt resolution.''

Jurgen Kaiser from Jubilee Germany suggested a more challenging way to solve the debt issue: ''Debtor countries should just repudiate the debt. The key lies in them refusing to pay debts and to stop negotiating in Paris – rather negotiate in African capitals.

''They should set the agenda for the meetings and stop paying the creditors who do not attend and insist on the meetings being chaired by the UN secretary general as a provisional chair,'' insisted Kaiser. – Reported by Stanley Kwenda from Harare for Inter Press Service on April 3. ☑

WOEFULLY INADEQUATE

(Continued from page 4)

However, the German development cooperation ministry (BMZ) does not agree with this general criticism. "The significant rise in social spending by post-decision-point countries is an indication that debt relief can make an important contribution to reducing poverty," BMZ says in a HIPC balance posted on its website.

The ministry says: In the countries that had received debt relief social spending rose from below 7 per cent in 2000 to 9 per cent of GDP in 2006. In Tanzania, for example, the government abolished primary school fees, built 2,500 new schools and employed 28,000 new teachers. The school enrolment rate in Tanzania increased from 57 per cent in 2000 to 95 per cent in 2005. Zambia and Uganda used the funds for spending in the health sector and abolished charges for primary health care. In Uganda demand for health services doubled as a result and the number of vaccinations also increased significantly.

BMZ notes that in order to bring further debt relief for these countries the World Bank and IMF are endeavouring to persuade bilateral creditors who are not members of the Paris Club, and commercial creditors of the highly indebted poor countries to take part in the debt relief initiative. "A particular challenge is posed by private funds which buy up HIPC debt and then sue the countries concerned in order to maximise repayments through the courts," it adds.

However BMZ is of the views that a definitive solution to the debt problem cannot be achieved through the HIPC Initiative alone. A country can be said to have a sustainable debt position only when it is able to service, over the long term and using its own resources, the external debt it requires for its development. "To achieve that a number of other measures are necessary, for example better terms of trade for poor countries so that their exports are competitive in the international marketplace and they can achieve higher earnings," the ministry points out.

Under the enhanced HIPC Initiative Germany is cancelling all reschedulable commercial debt and all debt arising from Financial Cooperation. Altogether debt relief will total up to 7.1 billion euros. By June 2008, 4.7 billion euros of that amount had already been cancelled. "By the time the Initiative ends, almost all HIPCs should then be debt-free vis-à-vis the Federal Republic of Germany." On top of that, Germany is compensating the African Development Fund (AfDF) and the International Development Association (IDA), the World Bank's concessional lending arm, for unpaid debt repayments. By the end of 2007 it had pledged a total of 165.5 million euros for the World Bank's HIPC Trust Fund. The Trust Fund helps smaller multilateral financial institutions in particular to finance their share of the HIPC debt cancellation initiative. Germany is also financing the HIPC Trust Fund through the European Union, which is supporting the Fund to the tune of 934 million euros. ☑