# Chapter 2

# THE RESPONSE OF AFRICAN GOVERNMENTS TO THE EXTERNAL DEBT

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## INTRODUCTION

The year 1982 was a significant landmark for the world's debt crisis, because in that year Mexico defaulted on its $80 billion debt to the West. The beginning of the 1980s also marked a general decline in the economies of the Third World countries, particularly of Africa. Beginning from the early 1980s, there was a worsening in the terms of trade for commodity exports, aggravated by the economic crisis of the leading capitalist economies. The minor economic gains, especially for the oil producing countries of Africa, were rapidly wiped out in the 1980s.

The terms and conditions under which African countries borrowed from the West were not favorable enough to allow for a smooth adjustment of African economies to the global crisis of the 1980s. As a matter of fact, the rigid conditions for loan servicing and repayment were strictly enforced because of the crisis. As a result, settlement of the loans by African Governments soon degenerated into a crisis. African debtor nations were required to set aside a rising percentage of their export earnings to service debts just when these countries' export earning capacity went into a rapid decline. In addition, these countries were denied access to international credit at a moment they needed such funding the most. Economic theory suggests that financial resources would normally flow from surplus to deficit families in order to stimulate investment and growth. Under the current debt crisis, resources flow from the deficit to surplus families, thus aggravating further the income gap between the rich and the poor. It is estimated that Africa's external debts stand at about $250 billion, with interest and capital repayment charges standing at about $30 billion per year. Given the estimated African population of 500 million people, it means that each African is today owing the outside world the sum of $500 or 7,500, for which he is required to pay the sum of $60 or 900 annually as interest and capital repayments.

Against the background of the low per capita income of less than $100, the African is left with little to survive on after meeting his external debt obligations. This situation degenerated from crisis to disaster in the late 1980s in the sense of declining domestic investment and incomes and increasing social unrest. By now the disaster appears headed for a catastrophe for the African. The production base appears to be collapsing. There is a rising mortality rate. There is the exodus of skilled and professional labour to the creditor countries precisely when such a labour force is required to salvage the economy. This catastrophic situation makes it rather difficult to initiate meaningful recovery measures against the background of rigid and unchanging international structures.

**AFRICAN RESPONSE TO THE DEBT SITUATION**

As indicated above, the debt situation has gone beyond a mere crisis, though the word "crisis" is employed in this discussion. It threatens the very economic and social fabric of the African people. It threatens the movement towards economic and social integration of the continent and seems to promise further disintegration of the continent if not handled with caution.

So far African Governments have, by and large, been the passive recipients of action programmes to deal with the debt crisis. In 1986, for example, the I.M.F. established a Structural Adjustment Facility (SAF) to provide funds for low income countries, with the terms and conditions for lending that deviated little from the traditional norms of I.M.F. lending. Earlier in 1985, the Baker Plan was introduced. In that plan, multilateral financial institutions and commercial banks were to increase their lending to some 16 highly indebted countries over a period of three years. Among African countries, only Nigeria, Morocco and Ivory Coast, were to benefit from the proposed $29 billion to be made available.

In 1987, a group of foreign creditor governments, the Paris Club, initiated a "Paris Club Plan" that requested the creditor governments to waive the repayments of past loans by converting them to grants on an approved economic recovery programme. The plan also recommended loan re-scheduling for longer periods of up to twenty years, provide such rescheduling did not include loans that were previously re-scheduled.

A number of other international initiatives have been contemplated. For example, in 1988, at the Toronto summit of the Group of Seven, debt write-offs and refinancing on soft terms were proposed, particularly of debts owed to the multilateral financial institutions. The Brady Plan of 1989 advocated debt forgiveness to heavily indebted countries as well as encouraging the I.M.F. and the World Bank to provide loans to international commercial banks with high degrees of exposure in the Less Developed Countries. In all of these international initiatives, however, the structures for lending and borrowing were assumed given.

On the African front, the Organization of African Unity (OAU) in 1987 adopted a common African stand on the debt problem. The Heads of State and Governments at the extraordinary summit in December, 1987, called for "bold initiatives and measures to deal with the structural nature of the African debt."

The views on the issue of the structure of the debt problem differ between the creditor countries and debtor nations. Creditor countries basically believe that the debt crisis arose principally because of the structures of the economies of the debtor countries. Debtor countries generally believe that the structure of lending as dictated by the Western creditors as well as other historical and economic relationships between Africa and the Western World account for the debt crisis.

The former view, however, prevails and has largely dictated the structure of economic recovery programmes generally referred to as Structural Adjustment Programmes (SAPs). SAP seeks to introduce market-oriented economic reform programmes in the debtor countries so as to enhance economic efficiency and international competitiveness to the advantage of the debtor countries.

Since the adoption of SAP in over 20 African countries, there have been major controversies between government economists and others regarding its success. The common ground for concern is that, whatever the success or failure of SAP, major macro-economic indicators, like investment, employment and output, appear to be on a long term decline. Inflation has remained strong. It can thus be concluded that major macro-economic variables witnessing negative trends cannot continue to be regarded as the side effects of SAP. This is why SAP, initiated in many African countries in the mid 1980s, has been undergoing further assessment and reforms since inception.

## SUGGESTED AFRICAN RESPONSE TO THE DEBT PROBLEM

The argument against the various responses of the international community to the debt problem is that they seek to keep existing structures intact. They enhance resource flows to debtor countries under the same lending conditions that created the debt crisis. They do not address the economic relationships that exist between the West and Africa and into which the structure of lending and borrowing fits. These reforms single out only the economic conditions of the debtor countries as responsible for the crisis. They focus only on individual countries, which must relate to the debtor countries solely through the spontaneous operation of the market forces. Hence, these reforms are heavily biased in favor of the creditor nations.

For example, the focus on the exchange rate as the key factor for reform and the subsequent devaluation of domestic currencies of the debtor nations has made it possible to shift the burden of the debt to the citizens of the debtor nations through the inflationary process. At the same time, the improvement in the current account of the balance of payments of some of the major debtor nations resulting from the devaluation, has made it possible to transfer large sums of foreign exchange earnings to service debts. When this situation is pitched against the background of declining foreign exchange earning capacity of the debtor country, it then becomes obvious why many African countries today are worse off than at the start of the crisis in the early 1980s. On the other hand, the net transfer of resources from the indebted African and other Third World countries generally, has made it possible for the international commercial banks and other financial institutions to adjust their finances in the last five years. In other words, the settlement of debts by debtors to Western creditors today spells, for the most part, windfall profits for the creditors, as most of them have already written off these debts in their books and appear to have fully adjusted their finances to these write offs.

The evidence for this assertion can be found in the secondary markets for debts instruments where a dollar debt instrument is sometimes offered for sale for as low as between ten to thirty cents. The direct interpretation of this development is that creditor banks can withstand non-repayments of the debts put up for sale to the tune of 70 to 90 per cent. It is not inconceivable, therefore, that most banks have successfully written off 100 per cent of their overdue loan repayments from Africa. This favorable development for the banks is not unconnected with industrial growth in the creditor countries of about 2.6 per cent in the 1980s. This industrial growth was enhanced by the net resource flows from the debtor to the creditor nations.

We must also note that internal conditions in most African economies contribute to the decline of African economies and thus further aggravate the debt problem. There are domestic misallocation and misappropriation of resources, poor prioritization and outright graft. The ever threatening political instability and the unwillingness of African leaders to accommodate opposing views have all combined to make long-term investment on the African continent precarious. Social and political instability on the African continent have made it nearly impossible for Africa to industrialize and guarantee the position as a weakened producer of primary raw materials.

The African response to the debt problem must therefore recognize the debt problem as part and parcel of the under-development problem. This underdevelopment has roots in Africa's colonial history and misrule since independence. The African response must also take account of Africa's objective towards growth and development.

On the *home front*, individual African countries must do the following:

1. Direct their annual budgets to more productive areas that will stimulate productive investment, reduce budget deficits and enhance per capita income, against the background of an articulated long-term national development plan.

2. Enhance people power in the administration of the country through the promotion of democratic institutions.

3. Give programmed priority to the mutual development of industry and agriculture.

4. Discourage the search for individual wealth by political office holders.

At the *continental level*, the African countries should attempt the following:

1. Form a Borrower's Club with the aim of influencing the terms of lending and borrowing from international sources. In this regard the Organization of African Unity (OAU), in collaboration with the Economic Community of Africa (ECA), should set up a specialized body to assist African governments in negotiating terms of international lending and borrowing. For each member of the Borrowing Club, any amount of borrowing from international sources with interest payments likely to exceed five per cent of the borrower's export earning capacity should be negotiated through

the Borrowers Club.

I consider defeatist the suggestion that African countries should stop borrowing internationally. It is not borrowing per se that is causing the debt crisis. It is the combined effect of the structure of lending and the misappropriation of borrowed funds that generates the crisis. Africa must integrate with the rest of the international community on terms that do not enslave its people. The collective surrender of Africa's sovereignty to the OAU will enhance Africa's growth and development more than will the surrender of each individual country to multi-national institutions.

2. Collectively ask for greater loan forgiveness, in view of the fact that SAPs have, in the main, assisted the international lenders to adjust to the debt crisis much better than the debtor countries have. The growing international understanding and cooperation should be extended to solving Africa's debt problems.

3. Ask for better representation at the decision-making level in many of the key multi-lateral institutions.

4. Re-kindle the debate on the New International Economic Order (NIEO) with a particular focus on the reconstruction of the IMF and the World Bank, so as to accommodate the legitimate aspirations of the African people and governments who are members of these multilateral institutions.