Chapter 4

ALTERNATIVES TO EXTERNAL DEBT

Eghosa Osagie

Another factor leading to the current debt problem in the case of Nigeria is the fact that Nigerians and their governments assumed that increases in the price of petroleum of the 1970s were permanent. This led to upward adjustment of our consumption standards. Our people demanded the best quality in products which were very often imported. The Governments granted excessively generous wage and salary increases, which bore no relationship to productivity of Nigerian workers. Contracts were routinely over-invoiced in the scramble to get unearned slices of the national cake.

When in the early 1980s, the price of crude petroleum fell from about $40.00 to less than $20.00 per barrel, Nigerians could not easily scale down their expensive tastes for high quality imports. The country had to resort to such short term borrowing as trade credits to maintain her undeserved consumption patterns. This inevitably led to rapid increase in the value of our external debt which now has to be serviced by about 30 percent of our foreign exchange earnings.

This situation creates problems for the country. For example, the rate of growth of the national economy is slowed down as foreign exchange, that should have been used to import machinery and equipment for industry, agriculture and transportation, are used to service foreign debts. The rate of unemployment increases. The rate at which our factories utilize their productive capacity is limited to low levels as factories do not have enough foreign currency to import needed raw materials. In addition, as has been observed in the 1980s, Nigeria has experienced great difficulty in servicing her foreign loans. This forced her to approach the major creditor institutions, the London Club and the Paris Club, for rescheduling, i.e. postponement of our repayment obligations. When external debt problems become formidable, we find it difficult to resist conditions imposed on us by the creditors, before they agree to reschedule our repayments.
They insist on massive devaluation of the naira, commercialization and privatization, reduction in public sector expenditure, leading to the premature retirement of public sector workers and on liberalization of the foreign trade sector. As a heavily indebted

country, we are forced to agree to these conditions, even though they create additional problems for us such as rising rates of inflation, unemployment, falling standards of living, particularly for salaried people, and very difficult conditions for small-scale industries, a great percentage of which go out of business. Rescheduling is not really a solution to external debt problem, as it merely postpones the evil day and actually increases the value of outstanding debt as interest obligations are routinely capitalized during the period servicing payments are suspended.

ALTERNATIVES TO EXTERNAL DEBT

As we have shown in the preceding section, a heavily indebted country finds herself in a difficult and even untenable situation. Some of the African countries experiencing serious external debt problems have asked the creditors for debt forgiveness and have even contemplated unilateral default. These steps are rather extreme and tend to adversely affect the credit-worthiness or credit rating of such countries. It is in consideration of these difficulties that we need to search for alternatives to external debt. We shall now consider some of these alternatives.

1. Good Balance Of Payments Policies

Foreign trade is normally financed with foreign currency. When we export goods and services, we are paid foreign currency. When we import, we expend foreign currency. If, as a result of inefficiency in production and undeserved high taste for consumer imports, we routinely import more than the export, we are said to be experiencing balance-of-payments deficits. This calls for adjustment, which really means reducing our consumption and imports. When we fail to adjust, balance-of-payments deficits result in reduction of our foreign exchange reserves. Since these reserves are limited and can actually run out, countries are, in the final analysis forced, either to adjust or to increase foreign borrowing. Thus the first alternative to external debt is a good balance-of-payments policy which helps to eliminate external deficits and the need to accumulate external debts.

Such a policy should ideally discourage unnecessary imports such as consumer goods which we can easily produce at home. If Nigeria had followed such policies in the 1970s, she would not have squandered her petrodollar earnings of the 1970s on the importation of rice, meat, sugar, milk, maize and champagne, and bleaching creams. Our "achievement" in this regard was unprecedented, and indeed a world record.

Economic analysis usually suggests tight fiscal and monetary policies to fight external deficits. Tight fiscal policies imply reduction in government expenditure, while tight monetary policies imply relatively high interest rates and restricted credit. While these policies may help fight balance-of-payments deficits, they may at the same time discourage production and in the process raise the level of unemployment.

Another balance-of-payments adjustment policy which is rather sensitive in its effects on the economy is exchange rate policy. Economic theory states that under normal conditions, devaluation (i.e., reducing the value of the local currency with respect to foreign currency) should <u>improve</u> the balance-of-payments position of a country. In other words, a country experiencing balance-of-payments deficits should devalue her currency for the external balance to improve. But when conditions are not normal, such a policy will not improve the balance of payments situation. Among the obstacles to such improvement are (a) the export sector is such that the value of exports cannot increase after devaluation, as is the case for a predominantly oil exporting country whose volume of oil exports is fixed by OPEC and the price quoted in US dollars and (b) when certain imports like machinery, equipment and spare parts have to be imported in order to produce goods and services. In some cases, such conditions may actually worsen it.

The possibility of such adverse conditions should make governments extremely cautious when introducing exchange rate changes. Extensive tests and calculations should be carried out by economists who have specialised in the field of international finance before such decisions are taken.

2. Inflow of Genuine Direct Foreign Investment

Another way of avoiding external debt is inflow of genuine direct foreign investment with long-term interest in the economy. The major difference between external debt and direct foreign investment is that external debt has to be repaid along with interest over an agreed period of time, while direct foreign investment requires the payment of dividends to foreign investors over the life-span of the project financed by it. If the project makes profits, dividends are paid, but when losses are incurred, the country has no dividend obligations to the investors.

The type of direct foreign investment desirable for a developing country is that which brings into the country modern technology which helps to produce goods that can be exported to any part of the world. The Far Eastern countries, like South Korea, HongKong, Singapore and Taiwan, have largely succeeded with this strategy. They put in place excellent infrastructural and telecommunications facilities and grant tax incentives to world famous companies with well established brand names to establish production plants in their countries. Their citizens seize the opportunity thus created to absorb the latest technology. The goods produced at relatively low costs are exported to the developed countries. This strategy helps the domestic economy to develop rapidly and enables it to avoid external debt problems.

3. Debt-Equity Swap

Another alternative to external debt is debt-equity conversion. This method has been experimented with by the Nigerian Government in the 1980s. This approach converts debt to foreign creditors into foreign ownership rights in Nigerian enterprises. Debt-equity swaps are usually conducted as follows. A foreign creditor holding a Nigerian debt instrument may decide to sell such instrument at a discount to another transactor, who in turn converts the instrument at the Central Bank of Nigeria into naira. He then uses the naira to buy up shares in existing Nigerian companies or to set up new enterprises. This transaction reduces the external debt of the country but increases by the same amount foreign ownership rights in the Nigerian economy. The choice is for the country to make.

CHANGE IN ATTITUDE OF NIGERIANS TO ECONOMIC ISSUES

It would be correct to state that the external debt problem is a symptom of a far more serious problem in the Nigerian economy. The overwhelming national ethic is dominated by an irrational and immoral craze to make money and to become wealthy overnight. Nobody bothers to ask anymore how people acquired their wealth. It is this unpatriotic attitude that made fraudulent bank officials to transmit large sums of foreign exchange into their individual accounts abroad in the 1970s and 1980s. It is this orientation that made Nigerians collude with foreign partners in the 1970s to import empty containers supposedly containing valuable machinery and equipment for which letters of credit had been opened and large liabilities recorded against Nigeria abroad. It is this spirit of economic immorality that induces private businessmen to keep part of their foreign exchange earnings in foreign banks, and public sector officials to over-invoice purchases abroad and contract costs in foreign currency so as to accumulate private bank balances in foreign banks. As has been argued by a leading Nigerian scholar:

> There is no doubt that the country has found itself in this predicament (of economic hardship) because of its poor financial management records and an almost complete disregard for accountability, both of which weaknesses have been successfully exploited to their advantage by self-interest seeking foreigners with the active collaboration of Nigerian nationals of doubtful integrity and tainted patriotism. (E. Inanga, Nigerian Journal of Policy and Strategy, Vol. No. 2, December, 1987, p.66).

This alternative to external debt is probably the most important for us. What is required is change of heart, a task in which our religious organizations have a leading role to play. If, as it is now obvious our current external debt problem is the result of economic mismanagement and self-centeredness in both the public and private sectors, it would be irrational to ask for debt forgiveness from foreigners when repatriation of foreign exchange held by Nigerians in foreign banks would wipe out all our external debt.

CONCLUSION

This paper has explored realistic alternatives to external debt. It briefly examines the causes and adverse consequences of our current external debt crisis. While recognizing good balance-of-payments policies, inflow of genuine direct foreign investment and debt-equity swap arrangements as realistic alternatives to external debt, the paper comes to the surprising conclusion that the external debt problem is a symptom of a more serious problem of wrong and unpatriotic economic attitudes of Nigerians. In the circumstances, the best antidote to external debt is good economic management, higher standards of economic morality and patriotism. The task of transforming Nigerians into more considerate economic actors requires the collaboration of our churches, mosques and traditional institutions.