I Background to the African Debt Crisis

1.01 The debt crisis, or perhaps more accurately, debt cancer [1] that has spread across Africa in the last decade, needs little introduction. Much has already been said about the causes, consequences and costs – economic, social, human and ecological – of that affliction and about the structural adjustment and economic reform measures which have been taken to cope with it on a continental scale. The reasons which gave rise to excessive African indebtedness in the 1970s and early 1980s, and which caused it to balloon from $140 billion when the crisis emerged in 1982 to over $270 billion in 1990, have been amply documented elsewhere.[2] It would be redundant to go into them at length again here.

1.02 Suffice it to say that Africa's over-indebtedness is not attributable, as many creditors would have it, merely to poor governance, rapacious and corrupt leaderships, protracted civil wars in too many countries on the continent; no democratic checks and balances on government borrowing and spending, excessive population growth, and the stubborn pursuit of economic policies which contributed to the relentless impoverishment of a rich continent for over two decades. All of these factors have indubitably

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1 It is odd to continue referring to a phenomenon which has lasted for over eight years as a crisis. It is more like a cancer because the debt disease has spread to virtually every corner of the continent; it has had a debilitating effect on the life of Africa's economies, and it is proving singularly resistant to cure by the remedies which have been attempted thus far.

2 For a detailed account of how the African debt crisis arose and developed readers are referred to: (1) "African Debt: The Case for Relief for sub-Saharan Africa" by Percy S. Mistry, Oxford International Associates, 1988; (2) "The External Debt of sub-Saharan Africa: Origins, Magnitude and Implications for Action" by Kathie L. Krumm, World Bank Staff Working Papers #471, July 1985; (3) "African Debt: The Search for Solutions" by Tony Killick & Matthew Martin, UNARP Briefing Paper no.1, June 1989. The causes, effects and possible solutions to the African debt crisis were the subject of an earlier Conference on "The Challenge to Recovery & Growth: Finding Solutions to Africa's External Debt" sponsored by the African Development Bank and held in London on April 18-19, 1988. The Collected Papers presented at that Conference provide useful source material, as do a host of country economic reports, special reports and working papers published by the UN Economic Commission for Africa, the World Bank and the International Monetary Fund. These are too numerous to single out for special mention.

played a major part. But Africa's crisis has been severely exacerbated by several other reasons as well, including:

(a) *thoughtless and irresponsible over-lending by private and official creditors,* during the commodity boom of the 1970s, without which irresponsible over-borrowing by African governments on this scale could not possibly have occurred;

(b) the *persistence of negative real interest rates during most of the 1970s* in global financial markets caused by lax monetary and fiscal policies in industrial countries which made it economically rational for developing countries to borrow externally (rather than save or attract equity investment) for development and consumption;

(c) the targetting of developing countries in general, and oil-exporting countries in particular, as major export markets to be provided with too-easy credit to *facilitate the adjustment of industrial countries to the two oil-shocks* (of 1973 and 1979);

(d) the *global monetary shock of 1979-81,* which aimed at ridding the world of inflation but had the collateral impact of inducing a deep and long recession, particularly in debt-ridden developing countries where the recession lasted for 70 months instead of 16 in the OECD world, and which caused commodity markets and prices to collapse;

(e) over-reliance on external savings between 1979-83 by *African governments' unwillingness to increase domestic savings and cut domestic consumption* in the erroneous belief [encouraged in some instances (e.g. Zambia) by the international financial institutions –IFIs] that the commodity price collapse would be short-lived;

(f) a *prolonged and devastating drought* between 1981-84 which severely impaired the continent's agricultural and cash crop production and resulted in extensive damage to output and to the financial structure of Africa's fragile economies;

(g) the emergence of *high, positive real interest rates throughout the 1980s* which compounded Africa's debt servicing and debt accumulation burdens;

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(h) volatile exchange rate movements throughout the 1980s with US dollar depreciation between 1985-90 resulting in increasing the dollar value of Africa's outstanding debts, over a half of which were denominated in currencies or composites which appreciated against the US dollar;

(i) *repeated official and private reschedulings*, often on punitive terms in the early years of the debt crisis, which resulted in further increasing the outstanding level of debt while providing temporary, but totally insufficient, cash-flow relief;

(j) *poor and impractical advice by IFIs and official creditors* on the extent of debt relief African governments needed to negotiate and how they might adjust, coupled with poor management by the same governments of external debt records, policies and priorities resulting in several missed opportunities to improve their situations;

(k) the *building up of egregious arrears* which creditors have tolerated to a point of doing more damage to restoring disciplined debtor-creditor relationships than if more sensible action to reduce debt and debt service burdens had been taken by them in the first place; and last, but definitely not least,

(l) *protectionism in the world's markets* for agricultural products and low-technology manufactures, which makes it particularly difficult for African countries to diversify and increase exports to hard currency markets, thus making it doubly difficult for them to earn their way out of the debt trap.

1.03 Several attempts have been made to explore the impact of these and other reasons more fully on the premise that unless the causes for Africa's predicament are properly understood, appropriate solutions will be impossible to design. It would be unproductive to revisit here what has been covered already elsewhere. There is now ample appreciation of the causes and the implications of Africa's debt burdens among its creditors, in the international community at large, and among quite a few (though unfortunately not yet all) of its governments. Indeed that has been the principal reason for creditors and donors having exerted considerable effort to deal with the problem much more seriously and responsively at least since 1987-88.

1.04 Success in achieving a durable solution has been elusive not because Africa's situation is inadequately appreciated or because there is lack of consensus on what the problems are and where the solutions lie. All creditors, even the reluctant and occasionally obstructive private banks, appear to agree that Africa's debt problem, *and particularly that of the low-income countries south of the Sahara,* needs special attention. It is generally accepted that the sub-Saharan debt problem is different to those of middle-income developing countries in North Africa, Latin America, Eastern Europe and the Middle-East. It is comparatively small *in absolute dollar terms.* Sub-Saharan debt is *less than a ninth* of the total external debt of all developing countries. But, in *relative* terms it has crippled, and unless tackled will continue impairing, the ability of African economies to reverse steadily declining per capita incomes. It is not widely appreciated that annual debt service burdens remain excessively onerous although *actual* payments of principal and interest by low-income countries in sub-Saharan Africa in 1990 were less than 37% of *scheduled* debt service (after repeated rescheduling). Yet, even at that reduced level they accounted for over 8% of the region's estimated GNP in 1990 and 28% of export earnings; implying that scheduled payments would have absorbed 22% of total sub-Saharan output and nearly 70% of its export earnings in that year!

1.05 If the causes and consequences of Africa's chronic over-indebtedness are so widely understood, what then is the problem? Why has movement towards a solution for reducing debt and debt servicing burdens to levels which fall within Africa's capacity to repay, and still leave enough by way of resources for investment and growth, been so slow and painful ? Why have African governments, their creditors and other external interlocutors not been able to act in a more resolute and meaningful fashion to reduce debt, as an essential precondition to achieving the modest 1% per capita income growth target which has become the standard by which low-income Africa's recovery efforts are now gauged? And why, after grant flows to Africa have increased from $6 billion in 1982 to nearly $12 billion in 1990, after debts totalling nearly $7 billion have been cancelled, and a further $1 billion swapped or converted in one way or another, have Africa's outstanding obligations continued to climb inexorably upwards ?

1.06 There are several answers to these questions. All of them shed some light on reasons for the glacial pace of progress which leaves Africa vulnerable to its immense potential remaining unrealized. But they leave a sense of dissatisfaction that the obstacles which remain cannot be overcome more quickly and decisively. Taken together they reflect poorly on the intentional, or inadvertent, inability of different "actors" in creditor countries – politicians, academic economists, senior government policy-makers, aid officials, treasury officials, export credit agency (ECA) officials, and so on – to exert the same enthusiasm and political will, as displayed in other instances closer to home, in relegating the African debt crisis to history; thus enabling countries on that benighted continent to get on with confronting the future without being dragged down by the debilitating encumbrances of the past. They also reflect the abject inapplicability and failure of the Paris Club debt rescheduling exercise which, though intended to help, may actually have seriously hurt Africa's debt situation and its prospects for recovery.

1.07 It is not easy, for instance, to explain the contrast between the urgency with which *politicians and governments in the industrial world,* and the Paris Club, responded to the crisis of Eastern Europe in the last two years and their negligent, almost desultory foot-dragging over the debt crises of Africa and Latin America over the last eight. Having repeatedly said that there were no public resources to devote to dealing with the debt problem, they found the money – over $13 billion – almost instantly to capitalize a new European Bank for the reconstruction of Eastern Europe; a bank whose *raison d'être* remains in doubt. Similarly the Paris Club, after repeatedly claiming that there was no political inclination in OECD countries, to go beyond the Toronto terms (explained later) applicable to Africa's low-income countries, turned around and recently concluded far more generous agreements with Poland and Egypt.

1.08 The reasons for the slow rate of progress in coming to terms with the clear need for rapid and large-scale debt reduction programmes for Africa – and low-income Africa in particular – are many. They include, among others: (a) perennial (and unjustified) concern on the part of creditors, especially commercial banks, that debt reduction for Africa on the scale necessary – no matter how justified it might be[3] – would serve as a precedent

3 This type of blanket concern about potential portfolio contamination contravenes the bankers' own insistence that each debtor case be treated on its own merits (the case by case approach). In Africa the case can clearly be made for most low-income countries that debt reduction on a large scale, with the burden of such reduction being shared by both official as well as commercial creditors, is absolutely necessary. That case has been made in all too many instances not by the governments themselves but by agencies like the World Bank and IMF.

for similar action to be taken elsewhere and thus weaken the bargaining position of banks in exerting pressure to maintain debt service flows from the developing world at unrealistically high levels; (b) the unfortunate reality that Treasury and ECA officials in OECD countries continually ride roughshod over the more intelligent, knowledgeable and sensitive views of their counterparts in aid ministries; (c) concern on the part of creditor governments, and of some people in the IFIs, that debt reduction would further exacerbate "moral hazard" by rewarding bad policies and behaviour on the part of debtors;[4] (d) the popular belief that debt reduction would release the pressure on forcing a more disciplined approach to overall resource management in African countries; (e) rather than helping disabled economies to recover debt reduction would only serve to line, to an even greater extent than now, the pockets of corrupt African leaders and civil servants in countries where graft has now become endemic; and finally (e) African governments have been insufficiently enthusiastic about embracing donor-advocated structural adjustment and policy reform prescriptions to justify large scale debt reduction.[5]

4 A corollary of this belief (and one which is unproven in reality) is that a tight, short-leash approach to debt relief, doled out grudgingly year by year in elaborate, expensive and tediously repetitive Paris Club reschedulings, provides greater and more effective leverage to creditors and IFIs in getting African governments to change the course of their economic policies and to endure with the consequences of such change.

5 This reason needs to be examined more carefully and seriously. In several African countries there is evidence emerging that governments have been cautious about proceeding with Bank and Fund adjustment prescriptions NOT because they enjoy being recalcitrant, or because they find such reforms to be politically difficult or administratively unworkable, but because the prescriptions are not resulting in the advertised cures. Exchange rate changes are not inducing switching effects at the pace anticipated. The lack of supply-side responses to changes in relative prices are leading to unstoppable cycles of inflation and continuous devaluation. Similarly resort to positive real interest rate policies in highly inflationary environments are causing a collapse in investment without any evidence of reviving savings. Swift trade liberalization is resulting in sharply widening current account deficits as imports race ahead of exports, and so on. Unless more credible and workable prescriptions are developed and applied, creditors should take a more realistic view about tying debt relief so closely to the speed of acceptance of untried and untested reform packages monitored by the Bank or IMF which have unintended and deleterious economic effects. A related point is the oft-repeated claim, particularly by the World Bank, that countries which have adopted reform packages are now performing better than countries which have not. The evidence, however, does not support such a clear cut conclusion. It is not clear whether these countries are performing better because of the reforms themselves or whether because their acceptance of reform has suddenly opened access to external financing which has enabled essential imports to be financed thus triggering growth. Also, the indicators of relative performance show such marginal improvements in the reforming vs non-reforming economies that they could easily be shown to be swamped by the fundamental inaccuracies inherent in the basic data available on African economies. Most of all this argument ignores the fact that reductions in actual (rather than scheduled) debt service payments from present levels could, in several instances, go a long way to improving economic performance even without significant policy change.

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1.09 None of these reasons ring true. Africa has, unfortunately, had to unilaterally "take" debt relief that should have been, but was not, "given" by running up levels of arrears which make a mockery of contractual arrangements and of the rescheduling process. In doing so it has paid a heavy price in terms of: a virtual cessation of normal trade credit; less assistance from donors for urgently needed commodity import and investment financing than it might otherwise have obtained; and a punitive premium of 30-40% on the price of goods that Africa imports.[6] As a consequence, prospects for recovery and sustainable development have been compromised even further. The shortage of imported inputs and intermediates – caused by the unavailability of trade credit and the absorption of scarce foreign exchange by exorbitant import price premia – inhibits better levels of agricultural output and of industrial capacity utilization from being achieved.[7] In the face of evidence to the contrary, the reasoning inherent in the reluctance of creditors to move expeditiously with debt and debt service reduction invariably leads to the mindless riposte that debt relief and reduction would not solve all the problems that Africa confronts. Nobody has ever suggested that it would. But, it is evident that if Africa's debt crisis were to be resolved once and for all, by reducing debt service burdens to around half of their actual (not scheduled) levels, the chances are now much greater than they have been for two decades that African recovery and growth would occur and could be sustained. Moreover, debt reduction on the scale necessary, would remove the last excuse that recalcitrant African governments might make in not embracing economic and political reforms more enthusiastically and speedily. The real costs to creditors in providing such relief are relatively small, but the potential gains to African debtors are so large as to make the risk worth taking.

6 This fact was established in a recent study undertaken by the World Bank, the findings of which were incorporated in a Working Paper entitled: "Does Africa pay more for its Imports - Yes".

7 The relationship between imports and growth in the African context is the most easily accepted, but the least understood, tenet of development faith. Evidence over the last 10 years shows no particular link between the value or volume of aggregate imports and of growth. Much more needs to be learnt about the structure and quality of imports relative to the productive capacity characteristics of particular African economies in order to be more certain about the link between increased import capacity, improved investment and growth performance.

1.10 With that introduction to a difficult and contentious subject the remainder of this paper considers in the sections which follow: the broad dimensions and characteristics of African debt and debt service; specific problems related to official *bilateral* debt and its rescheduling; the growing problems of meeting debt service obligations to *multilateral* institutions, particularly the IMF and World Bank; and the implications of not being able to clear the overhang of debt owed to *privat*e creditors. The paper discusses the initiatives which have been taken and those which are presently being considered, to reduce the African debt burden further in each of these different types of debt categories and highlights areas where more could be done. It concludes that just as war is too important to be left only to generals, debt is too important to be left only to Treasury and ECA officials from creditor countries, and to IFIs, to deal with. Its resolution requires more consciousness and commitment on the part of politicians in the developed world because the solutions now lie in the realm of politics rather than that of economics and finance.

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