

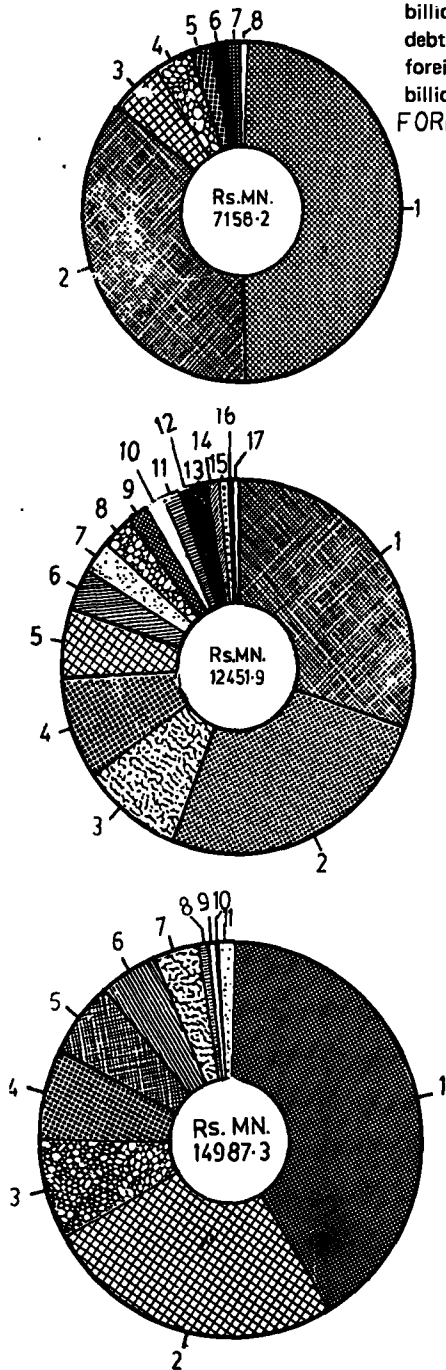
AID DEMAND AND FOREIGN DEBT

A vulnerable balance of payments has been one of the crucial features of the Sri Lankan economy. This is reflected most strongly in the external resources gap that has continued to grow in recent years. Lead projects such as the Mahaweli, the Urban Development Programme and the FTZ; together with the liberalisation of the economy after 1977 have all resulted in unprecedented demands for foreign resources. To keep liberalised trade moving freely more and more had to be imported, but with export earnings not keeping pace, the country's merchandise trade gap has reached record levels.

Sri Lanka's balance of payments has continued to deteriorate creating a resources gap that has demanded even more foreign assistance and pushed up the foreign debt to new highs, as these diagrams illustrate. This has become a major issue confronting the national budget and the entire economy..particularly, if the pace of development initiated in recent years is to be maintained. How to limit expenditure, both local and foreign, while raising revenue has become the key issue, and closely linked to it are the problems connected with balance of payments and foreign resources.

For the first time in the history of the country's public debt in February 1983, the foreign debt (net) moved ahead of the domestic debt (net) with foreign reaching Rs 38.3 billion and domestic at Rs 37.9 billion. By October 1983 the domestic debt (net) was 39.9 billion while the foreign debt (net) had moved up to Rs 44.1 billion.

FOREIGN DEBT OUTSTANDING—1982



OTHER LOANS

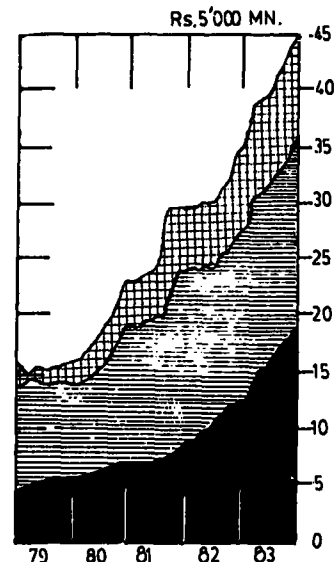
1. EURO CURRENCY
2. I.M.F.
3. O.P.E.C.
4. JAPAN
5. U.A.E.
6. IRAQ
7. CHINA
8. INDIA

PROJECT LOANS

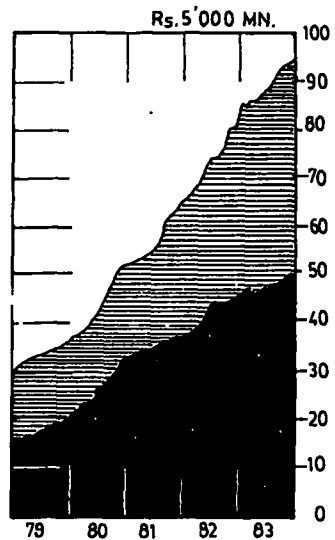
1. I.D.A.
2. A.D.B.
3. F.R.G.
4. CANADA
5. U.S.A.
6. CHINA
7. KUWAIT
8. JAPAN
9. I.B.R.D.
10. SALMON BROTHERS INCORPORATED N'Y
11. O.P.E.C.
12. NETHERLANDS
13. I.F.A.D.
14. U.S.S.R.
15. INDIA
16. DENMARK
17. SKANDINAVISKA ENSKILDA BANKERS SWEDEN U.A.E. G.D.R. & SAUDI ARABIAN FUND

COMMODITY LOANS

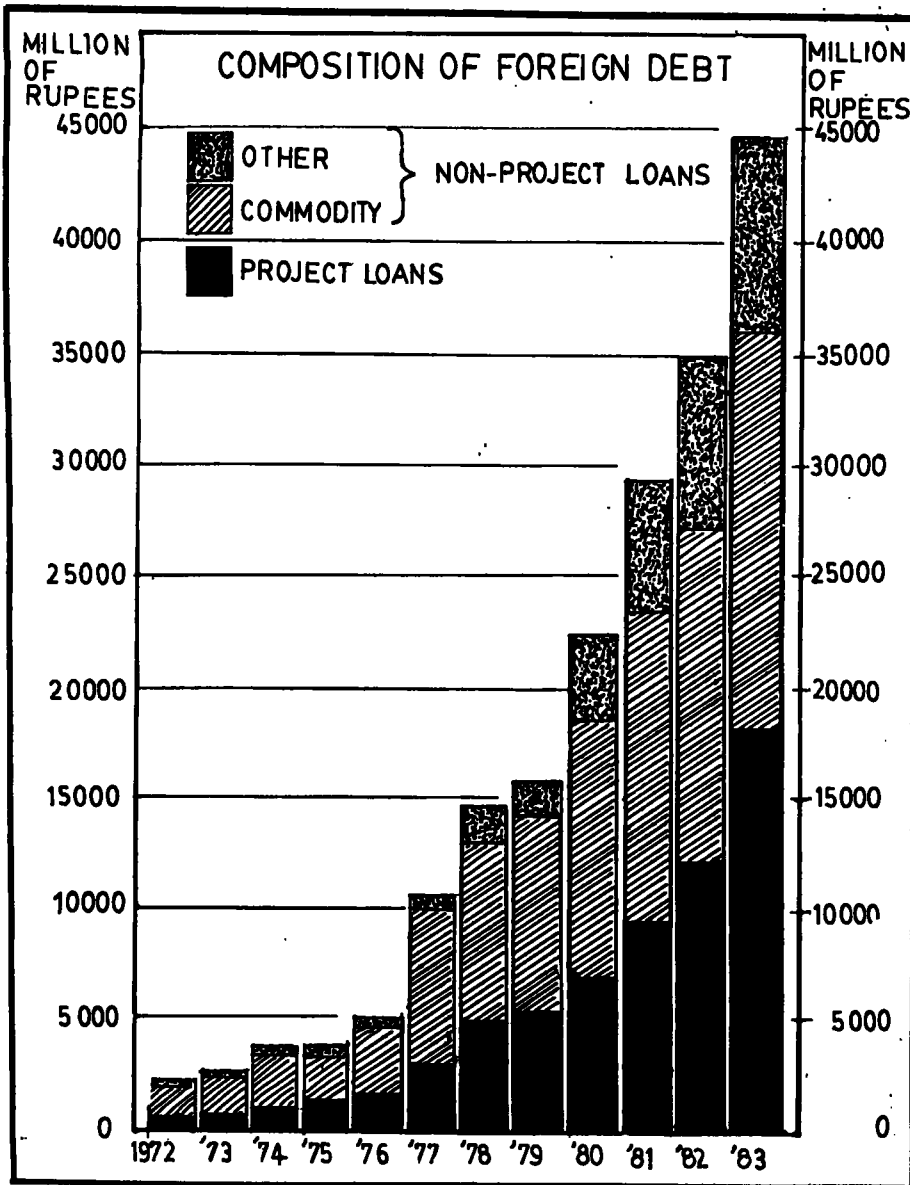
1. U.S.A.
2. JAPAN
3. NETHERLANDS
4. CANADA
5. FRANCE
6. F.R.G.
7. INDIA
8. DENMARK
9. CHINA
10. U.S.S.R.
11. SWITZERLAND HUNGARY & ITALY.



- OTHER LOANS
- COMMODITY LOANS
- PROJECT LOANS



- FOREIGN DEBT
- DOMESTIC DEBT



world picture began to change throughout the 20th century as a result of a series of key global events. Some of these events were: the First World War, a partial consequence of which was the establishment of the Soviet Union as a separate economic entity; the world depression of the 1930's leading ultimately to a Keynesian prescription of giving purchasing power by fiscal means to the poorer sections of the Western economies within the capitalist framework; World War 11, following which began a decolonisation process leading to the emergence of a large number of independent countries in the Third World, as well as the emergence of further territorial units under the socialist system. The post World War 11 world of newly independent countries wrought new relationships in trade and in aid, dependent of course on the broader geopolitics of the world and attempts at development in the Third World.

The Soviet Union under a different social system was the 20th century heir to the earlier Russian Empire with its conquered lands in the Asian region. Being under a single government the development assistance to the Asian hinterlands was not considered aid, and the gross disparities between the Asian and European parts of the Soviet Union have been lessened through successive development plans.

Aid in the Western world occurred first under Marshall Plan assistance to Western Europe which was a response to both the excesses of the Soviets under Stalin and the anti communist hysteria after the Second World war. Marshall aid from America led to, for example, the West German recovery in the 1950's although it did help in the long run decline of Britain as a major power.

Apart from the Marshall Plan there were multi-lateral agreements arrived at by capitalist countries (at Bretton Woods) to stabilise the world economy, so that a depression like that of the 1930's would not recur, which had mechanisms for transfer of funds. The result was the birth of the International Bank for Reconstruction and Development, and the IMF. (See box) America with a mixture of strong self interest, as well as a liberal self-enlightenment (largely coming from its Democratic Party) became a major aid giver. However, quite often some of the aid packages were strongly conditional in the hysterical anticommunism of the 1950's. This was the time of John Foster Dulles, Mc Carthy and congressional hearings on un-American activities, facets of American political behaviour which have been regretted by subse-

FOREIGN AID AND DEBT

Foreign "Aid", including loans, has received considerable comment in Sri Lanka. This 'Special Report' hopes to identify some of the major dimensions of the aid process and its impact on the Sri Lankan economy. Since aid, both grants and soft loans, are from foreign countries, a consideration of aid is not possible under the international background of aid is also taken into account.

International Background

The need for aid arises in attempting to bridge the resources gap between the developed and developing countries. The aid relationship is an unequal one which is not easily accepted by people in both

donor and recipient countries. In our previous issues we have touched on the reasons for the present inequalities in the world system. Broadly, they are the use of high productive technology in the developed countries, combined with an unequal economic order which have historically governed the system of exchange of goods and services at the international level.

The 19th century saw a rapid industrialisation of Europe and a differential growth between the newly industrialising countries in Europe and their appendages in the colonies which were both suppliers of raw materials and of markets. This dominant

THE WORLD BANK AND IMF

The World Bank and the International Monetary Fund were two separate but complementary agencies set up, at the initiative of the Western industrialised nations, at the end of the Second World War with the intention of rehabilitating a world economic system that was in a state of collapse. All the European economies had been largely exhausted or destroyed after the war. The memories of the monetary turmoil of the capitalist countries in the 20's and 30's was still fresh and concern about a possible recurrence was widespread. These memories and concerns, prompted the major Western nations to convene at Bretton Woods, New Hampshire, USA, in July 1944, in order to find a workable solution to the task of international economic reconstruction. The outcome of this conference was a comprehensive blueprint for setting up two international agencies, the IBRD and the IMF, which were to exert their influence on the World Economic Order ever since.



The World Bank (IBRD) was established in December, 1945 following the Bretton Woods Conference, where the major nations met to design a workable International Monetary System and set up an agency through which war-torn Europe could be restored with long term loans. The International Bank for Reconstruction and Development, as its name implied, was thus established primarily with this end in view.

From the 1950's however, the Bank directed most of its financing to development projects in the Third World and is today regarded as the world's leading international institution for development financing. From the 28 countries which signed the Articles of Agreement drawn up at Bretton Woods in July, 1944 its membership has now risen to 132 countries each of which subscribes to the Bank's capital base. Over the years its sub-agencies the IFC and IDA were brought into the World Bank to provide more specialised forms of financing to the developing world.

The original purposes of the IBRD were "to assist in the reconstruction and development of territories of members by facilitating the investment of capital for productive purposes; to promote private foreign investment, when private capital is not readily available on reasonable terms; to supplement private investment by providing loans for productive purposes out of its own capital funds realised by it and its other resources; and to promote the balanced growth of international trade and the maintenance of equilibrium in balances of payments by encouraging international investment for the development of the productive resources of the Bank's members"

The IDA, which came into existence on September 27, 1980 and whose administration is the responsibility of the World Bank was set up "to promote economic development, increase productivity and thus raise standards of living in the less developed areas of the world, included within its membership, by providing finance to meet their important development requirements on terms which are more flexible and bear less heavily on the balance of payments than conventional loans such as those of the IBRD and IFC."

Its assistance was to be concentrated on countries regarded as very poor — mainly those with annual per capita incomes of less than US \$ 300. This association was intended to further the developmental objectives of the Bank and supplement its activities.

The other agency of the World Bank, the IFC, was set up a few years earlier. Though established in July 1956 it became a specialised agency in relationship with the United Nations in February, 1957. While closely associated with the World Bank, the IFC is a separate legal entity, and its funds are distinct from those of the Bank.

Its main purpose is "to further economic development by encouraging the growth of productive private enterprise in its member countries, particularly in the less developed areas."

The IFC pursues its objectives by investing in productive private enterprises, in association with private investors and, without Government guarantees of repayment, in cases where sufficient private capital is not available on reasonable terms; serving as a clearing — house to bring together investment opportunities, private capital (both foreign and domestic), and experienced management; and helping to stimulate the productive investment of private capital, both domestic and foreign.



The International Monetary Fund (IMF) is sometimes confused with the World Bank or one of its agencies. It must be made clear that the IMF was set up as an Organisation that would be responsible for the new Monetary System that was established in December 1945 at Bretton Woods.

The IMF's objectives were thus clearly defined as follows:

"to promote international monetary co-operation and the expansion of international trade; to promote exchange stability, maintain orderly exchange arrangements and avoid competitive exchange depreciations; and to assist in the establishment of a multilateral system of payments in respect of currency transactions between members and in the elimination of foreign exchange restrictions which hamper trade."

The functions and operations of the IMF were such, that they invariably have resulted in the Fund laying down rigidly its terms to governments seeking its assistance, and the measures it has recommended have not been popular in these countries. This has led to much criticism of the IMF, among some of these countries, who in balance of payments difficulties have been compelled to seek the fund's facilities. The World Bank, on the other hand, with its more populist stance, particularly after the Nairobi sessions in 1973 has, in recent years, come in for less criticism than the IMF.

The World Bank has over the years directed a major part of its loans to commercial and infrastructure development, particularly large scale projects like electric power stations, railways, ports, hotels, mining and manufacturing installations, development schemes, roads, highways and other urban and rural settlements, agriculture and integrated rural development schemes. In 1973 the Bank gave notice that it was making a complete change in policy, and lending patterns and redirecting its programmes with the intention of raising the productivity of the poor and enabling a greater transfer of resources from the more developed to the less developed countries. The occasion was

the Annual Meetings of the World Bank and IMF in Nairobi in 1973, when Bank President Robert S. McNamara made his address. Many critics have maintained, however, that the money from the World Bank has not gone to really help the poor people although its activities have been carried on in the name of the poor. "Its been done in the name of the poor, but when you look over the projects there's very little evidence that it's ever really done anything to the poor," said Clarence Long of the US House of Representatives commenting on World Bank assistance. This criticism of the World Bank caused a certain amount of resentment within the Bank towards the US Congress for what it considered "unwarranted attacks upon successful attempts to assist the poorest of the poor." This is part of the debate that has gone on in recent times concerning the fundamental nature and purposes of the World Bank. These basic issues have been set out more simply in the following questions.

Is the World Bank a bank with traditional banking concerns whose object is to make a profit by ensuring an adequate return on its lending and investments? Or is it a development agency with the goal of underwriting those projects most likely to promote economic and social progress among the poor? Or can the Bank successfully accomplish both objectives simultaneously?

Bank officials maintain that their's is an international lending agency which provides critically needed development capital to the Third World with a view to solving the problems of mass poverty. They are doing so by funneling billions of dollars in aid to development projects which are likely to be financially successful. Their sole object, it is claimed, is to assist the poor to become more productive, through such assistance; but with no political strings attached.

The critics argue, however, that the World Bank, by its very nature, is political, since it is controlled by the financial elites of the world's leading capitalist countries. The Bank, according to this view, helps to maintain the prevailing financial, economic, political, and social order of the Third World — and indirectly, the First World — at the expense of the aspirations of the poor. As presently structured and governed the critics maintain that the Bank may be an excellent bank, but many questions are raised as to whether it can operate effectively as a development institution. For instance, the planning of several bank projects

quent enlightened generations. One such aid package was the Point Four Aid Programme which was conditional on four points.

However circumstances both within the Western countries, as well as in the world at large have changed aid policies. One of the key turning points in aid policy was in the 1970's. This change affected aid policies not only in multi-lateral agencies like the World Bank but also bi-lateral aid. The World Bank under McNamara instituted a concept of aiding the bottom 40 percent of the population of recipient countries and also looking with favour at countries with good income distribution records. This was an important change for countries such as Sri Lanka.

Earlier Sri Lanka's welfare policies had been frowned upon by successive IBRD missions and Sri Lanka's efforts were considered an example to be avoided. However, in an important document issued by the World Bank in the 1970's titled "Distribution With Growth", Sri Lanka was singled out as a good example because of its income distribution which depended on welfare policies. This change of attitude in the World Bank under McNamara could probably have occurred because of the changed geopolitics at the time, such as McNamara's reticence on America's loss of the Vietnam War. — McNamara being a key decision maker at the early period of the War.

These changes were also assisted by the changed social climate in America at the time which was characterised by a greater feeling for the deprived and dispossessed both in America and elsewhere. Similar changes in lending policies were reflected in the direct US aid policies under Carter, who bringing in a humanitarian perspective took perhaps the most pro-Third World stance of any American President so far. He also changed the conditionality of aid so as to take into account factors such as democracy and human rights. These changed aid policies of the mid 1970's were most reflected in new aid policies of say the Dutch, the British and the Scandinavian countries. These new aid policies all emphasised such factors as income distribution, some degree of democracy and popular participation in the recipient countries. On these counts, by the mid 70's, Sri Lanka had become a major candidate for foreign aid under favourable terms and conditions. It had a fair income distribution a fair record of democracy and a generally good human rights record.

AID FLOWS

The developing countries obtain their foreign "aid" in the form of grants or loans through two channels; bilaterally and multilaterally. The bilateral aid is what flows between two countries from one donor country to a recipient, or from the export credit agency of a particular country; Multilateral aid flows from the international agencies to the individual countries.

The multilateral organisations which play a major role in disbursing foreign loans and aid are the specialised agencies under the United Nations such as the FAO, UNIDO, WHO; the World Bank Group's International Bank for Reconstruction and Development (IBRD) and the International Development Agency (IDA); the International Monetary Fund (IMF); the regional banks such as the Asian Development Bank (ADB) the funding agency of the Organisation for Petroleum Exporting Countries (OPEC) and the development assistance committee of the Organisation for Economic Co-operation and Development (OECD).

The International Development Strategy of the Second United Nations Development Decade specified that each economically advanced country should provide resource transfers (including private flows), amounting to 1 percent of their GNP's annually, to the developing countries. Within this 1 percent it set 0.7 percent as a target for official development assistance (ODA). Although the 1 percent norm for overall net flows (including private investment and commercial lending) has been reached, the ODA target has been left behind. The net total of all types of financial resources (bilateral and multilateral) from all sources (DAC, OPEC, and CMEA countries) received by developing countries in 1982 amounted to over \$ 100 billion. Of this an estimated 88 percent was from the OECD countries about 9 percent from the OPEC members and 13 percent from the CMEA countries. Net ODA disbursements (1981) were only \$ 35 billion of which 72 percent was from the OECD countries, 22 percent from the OPEC members, and 6 percent from the CMEA countries. The total net aid flows from the OECD's 18 Development Assistance (DAC) countries in 1973 was US \$ 24.8 billion and the if at that time the 1 percent target was to have been met additional transfers totalling US \$ 6 billion would have been required. The OECD's member countries have been major aid donors and in 1973 they accounted for 90 percent of total bilateral flows (excluding Euro currency loans)

while these same countries accounted for nearly 90 percent of the financial resources made available to multilateral institutions. However, total aid as a proportion of gross national product from DAC members has remained at around 0.35 percent over the years and in 1981/82 it was 0.37 percent which was the same level they reached in the late 1960s. This is regarded as a deeply disappointing record.

\$ 566 million or 1.01 percent of GNP. In 1982 Denmark reached 0.77 percent, France 0.74 percent, Belgium 0.59 percent and Australia 0.57 percent. The United States contribution has kept falling from the original 0.5 percent it made in 1960.

The OPEC countries have, with their increased oil revenues in recent years, contributed nearly 3 percent of their GNP. Ten of the thirteen OPEC Members

share of their GNP, OPEC aid rose from 1.18 percent in 1970 to almost 3 percent in 1975 but declined afterwards to 1.4 percent in 1981. The aid/GNP share of the Arab Gulf countries however, was substantially higher (3.85 percent in 1981).

Net aid disbursements of the CMEA countries (Bulgaria, Czechoslovakia, GDR, Hungary, Poland, Romania and USSR), estimated by the OECD Secretariat, were small compared to other donor groups, accounting for about 6 percent of total ODA received by the developing countries and multilateral institutions in 1980 and 1981. (See table 1) On the basis of available information the OECD Secretariat estimates that the ratio of ODA to GNP for the USSR was probably 0.13 percent in 1981 and 0.12 percent for the East-European countries. These figures on aid do not include the preferential trade prices offered to Cuba and Vietnam by the USSR since price subsidies are not considered to be a part of ODA by the OECD's Development Assistance Committee.

Also, the CMEA countries have held the view that underdevelopment of most of the developing countries is a legacy of the colonial past, and therefore it should not be their responsibility to aid these countries. Thus CMEA aid in conventional terms, is comparatively small and is compensated for through the bilateral trade and technical assistance agreements many of the CEMA countries have with the Third World. There is also a degree of assistance that goes out from the USSR to other CMEA members, both in the form of capital and trade credits.

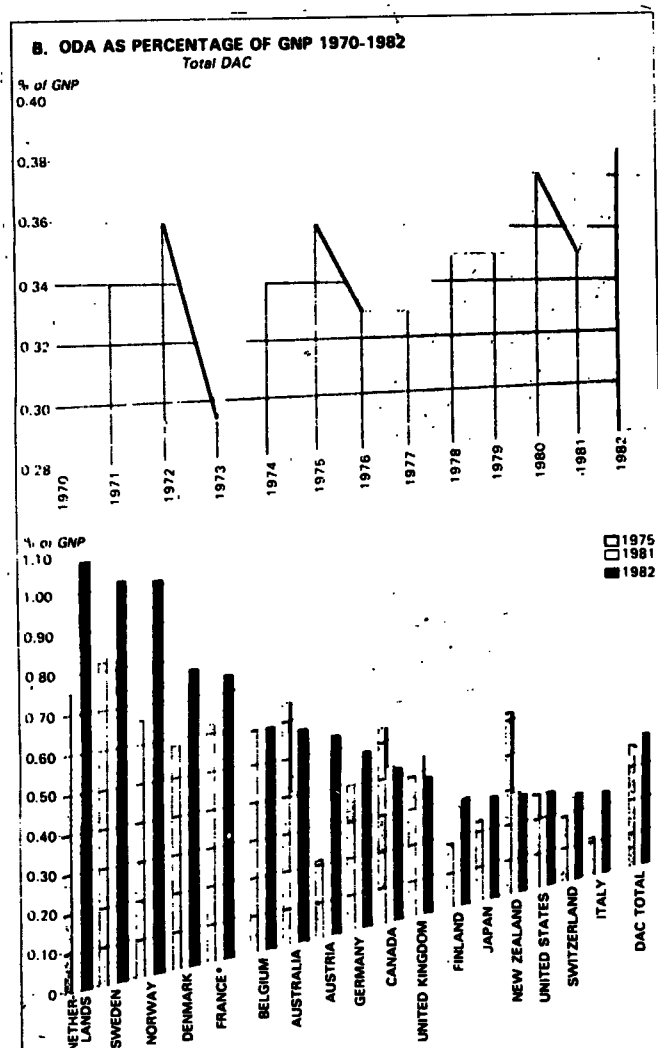
An examination of the bilateral aid flows by their geographical pattern reveals some interesting facts about the interests of donors. Sixty percent of technical assistance from France has gone to its current and former dependencies. Japan which has emerged as an industrial giant and a major donor, has shown a preference towards assisting Asian countries (52.7% in 1980 to Asia), especially Indonesia. Though widely distributed, U.K. aid has gone mainly to its former colonies.

Seventy five percent of aid from Saudi Arabia was directed to countries of the Arab world. Kuwait has also channelled 50 percent of her aid to Arab countries. The situation is similar regarding UAE aid.

USSR assistance has been mainly to Vietnam, Cuba, Afghanistan and other COMECON countries.

Australia aid was diverted mostly to Papua New Guinea (60%), South East Asia (20%) and the Pacific countries.

Fifty per cent of Belgian aid has gone to Zaire, Rwanda and Burundi its former colonies.



Even among OECD members (as seen in the diagram), there were exceptions in the Scandinavian countries and the Netherlands, which exceeded the target. The Netherlands in 1982 exceeded the 0.7 percent of GNP target for the eight consecutive year, repeating the record level of 1.08 percent reached in 1981. A new record level was reached by Sweden in 1982 with an increase in its net ODA outflows of one third in national currency; which brought the dollar value of Sweden's aid to almost a billion dollars, corresponding to 1.02 percent of GNP. Norway reported a 36 percent increase of its ODA in national currency (23 percent in real terms), carrying its net ODA disbursements in 1982 to

started to provide substantial financial assistance to other developing countries soon after the major increase in oil prices in 1973/74. As early as 1973, OPEC countries had replaced the CMEA donors as the second largest donor group, with a share of 16 percent of world ODA. Some OPEC donors had provided financial assistance to a few developing countries well before that year, but the absolute amounts were modest compared to new aid levels. The share of OPEC donors in total aid disbursed by the three main groups of donors increased continuously from 5 percent in 1970 to 30 percent in 1975 but fell in the following years to reach 22 percent in 1981. Likewise, as a

Chinese aid went mainly to North Korea; while West Germany, Canada, Sweden, Norway and the Netherlands have adopted a more widespread pattern covering the poorest countries of the Third World. During the 1976-1979 period total ODA (Overseas Development Assistance) received by the aid recipients in Europe, South and Central America, Africa, Middle East and Oceania was \$ 21,235 million, out of which \$ 5,217 were through multilateral donors \$ 12,156 million from OECD and \$ 3,862 million from OPEC. These figures exclude overseas development assistance from the centrally planned economies of USSR and Eastern Europe.

The medium and long term debt of the developing countries increased by 20 percent a year in the 1970's, while increasingly larger resources were needed to service this debt. The position changed after 1980 with the rate of growth of debt being halved to an estimated 11 percent; but by 1982 the slow down in export earnings for these countries was even sharper. As a result the ratio of debt to export rose from 76 percent to 104 percent between 1980 and 1982; and if short term debt is included this ratio would have exceeded 150 percent. For the oil importing developing countries this ratio was higher than at any time since 1970. One factor that added heavily to this debt

burden was that since a large part of developing-country debt is denominated in dollars the appreciation of the dollar in foreign exchange markets aggravated the situation.

The way developing country debt evolved in the 1970's left most of the borrowers vulnerable to the pressures of the early 1980's. A significant factor of the growing debt situation was the tendency for developing countries to resort to more private sources, as official inflow of development assistance was slowing down. By increasing their net short term debt these countries also became more exposed to rising interest rates and to sudden withdrawal of support by Commercial Banks.

Although international capital markets were expected to increase their medium and long term loans to the developing countries, there were doubts whether this would be sufficient to cover the increasing requirements of interest payments on outstanding loans. These countries therefore had no alternative but to resort to private sector flows such as direct investment, export credits and short term borrowing, and urgent official capital flows, including credits extended by the International Monetary Fund.

An UNCTAD study has predicted that among the means of financing will be official flows with varying degrees of concessionality and conditionality; and these flows will continue to finance about 40 percent of the current account deficits of developing countries. The study adds that the high levels of debt and debt service relative to export earnings "will continue to render many developing countries highly vulnerable to sharp fluctuations in their export earnings or to abrupt changes in market perceptions of their credit worthiness. The total outstanding medium - and long-term debt of developing countries other than major oil exporters is expected to reach \$539 billion by the end of 1983, amounting to 135 percent of export earnings, compared with 121 percent in 1981. The inclusion of short-term debt, about which information is extremely tenuous, could add as much as \$ 100 billion to this

Table 1
Aid Donors - OPEC, CMEA and DAC
Comparative Volume Performance (Net ODA disbursements)

		OPEC	CMEA	DAC	Total
S billion	1970	0.4	1.0	6.9	8.3
	1975	6.2	1.2	13.8	21.2
	1980	9.1	2.2	27.3	38.6
	1981	7.7	2.1	25.6	35.4
% of GNP	1970	1.18	0.14	0.34	-
	1975	2.92	0.07	0.36	-
	1980	1.70	0.14	0.38	-
	1981	1.40	0.13	0.35	-
% of total ODA	1970	5	12	83	100
	1975	30	3	67	100
	1980	23	6	71	100
	1981	22	6	72	100

Comparative Terms Performance

Grant element of loans %			Overall grant elements %		
1975	1980	1981	1975	1980	1981
47	49	52	72	80	80
50	52	57	52	65	70
63	59	58	89	90	89

Source: OECD Secretariat Data

The external debt problem of the developing countries grew progressively from the late 1950's and increased rapidly in size during the 1970's and early 1980's. The net oil importing developing countries have been most affected, particularly in their debt service payments as well as capabilities to raise further foreign capital. The table at night shows the growing proportion of foreign debt that all developing countries faced over the years.

Table 2
All Developing Countries Outstanding Debt Outstanding
(Billions of Dollars)

	1970	1980	1981	1982
Total Debt	50.4	334.4	398.1	466.6
Debt Service % of GNP	1.8	3.4	4.1	4.7
Debt service as % of Exports	13.5	13.6	16.3	20.7

Source: World Bank, UNCTAD

figure. The net outstanding and disbursed medium-term debt of major oil exporters is also large in absolute terms, although small in relation to export earnings. Inclusion of this debt, which is expected to reach \$ 125 billion by 1983, would lead to a projection for the net outstanding and disbursed medium- and long-term debt of all developing countries of \$ 600 billion by the end of 1983".

Increasing Third World Debt

Towards the mid 1970's the international community was compelled to display increasing concern over the problem of the Third World debt and the monetary issues associated with this problem. The Seventh Special Session of the UN General Assembly, held in September 1975, set out a framework for international co-operation in several vital areas. In recognising the importance of the debt problem and financial needs of the Third World this Session stated "The debt of the developing world is increasing to a point where their import capacity as well as their reserves have come under serious strain Developing countries should be granted access on favourable terms to the capital markets of developed countries"

The agitation continued to the end of 1980's and when the Non-Aligned Nations held their summit meeting in Havana, in 1979, those Heads of State and Government present expressed deep concern about the existing monetary system which they felt was "not responsive to the development needs of the non-aligned and other developing countries and had resulted in many cases in the increase of their dependency, and a continuous deterioration and weakening of their economies".

In an "Economic Declaration" the Heads of State emphasized that "the international financial situation was increasingly characterized by, *inter alia*, factors such as unstable exchange rates, generalised inflation, disorderly creation of liquidity in the international money markets, and inadequate creation and inequitable distribution of liquidity by international multilateral agencies, the prevalence of the main developed countries which control the monetary system in the decision-making process and, in general, its lack of responsiveness to the needs of the developing countries".

The crisis was mainly one of liquidity for several developing countries, though it could not be isolated from other inter-related problems that were effecting the developing world. The most apparent of these problems were the acute disad-

vantages the Third World faced in the International Monetary and Trading Systems.

The crisis was mainly one of liquidity for several developing countries, though this sector could not be isolated from other inter-related problems that were effecting the developing world. The most apparent of these problems were the acute disadvantages the Third World faced in the International Monetary and Trading Systems.

The inequities in the global economic system which have led to the economic and technological development of some and to the underdevelopment of other parts of the world have been the subject of much discussion. The inequitable and unfavourable international economic environment that has resulted was summed up effectively by Indian Premier Indira Gandhi in a recent address to her Congress Party sessions as follows: "*Colonialism has ended but the industrial countries still account for 80 percent of the world's income, 90 percent of the technology and 82 percent of the world trade. The unequal strength between the developing and developed is illustrated by the fact that the exports of 12 commodities fetch \$ 30 million to the developing countries, but the developed earn \$ 200 million by processing these same commodities. We are always reminded of the aid that developing countries receive. The total of annual aid stands at \$ 20 billion, while the annual military expenditure is \$ 680 billion*".

A traditional disadvantage faced by the Third World countries is that they usually have to pay for their imports in "hard" currencies of the Western industrialised nations. This traditional disadvantage was aggravated from the early 1970's with the break-down of the Bretton Woods international monetary system after which exchange rates of "hard" currencies were no longer pegged to the gold exchange standard and have therefore continually fluctuated. The weaker economies of the developing world were most seriously effected by this trend of monetary instability.

In an effort to reduce dependence on the US dollar, and provide an orderly increase in official reserves, and also move towards a stable and more permanent international currency Special Drawing Rights (SDRs) were created through the IMF in July 1969. This was the first attempt to create international liquidity through deliberate decisions of the international community. But the SDR's were allocated in proportion to the contributions and quotas each country had with the IMF and therefore the bulk of the SDRs have gone to the industrialised Western countries. (Between 1969 and 1974 only

28 percent of SDRs were allocated to the 99 Third World countries in the IMF while the other 27 most developed received 72 percent).

The other associated problem area has been the deteriorating terms of trade which have undermined the developing world's liquidity situation. The trade of the developing countries has been affected by wide price fluctuations, falling demand and increased protectionism in the developed world markets; while inflation and the economic slow-down in the industrialised countries has also increased the prices of Third World imports over the years.

The major fault was traced to the Bretton Woods System and the financial agencies it setup which had no mechanism to discipline the liquidity surplus countries; for instance, by obliging them to import more or to lend favourably to deficit countries. Critics of the system pointed out that the IMF extended credit to deficit countries only on conditions regarding their policies affecting government budgets, money supply, the exchange rate and trade restrictions. Thus, when a deficit country suffered a loss of reserves and appealed to IMF for help it was forced to adjust on IMF terms, whereas accumulation of reserves by a surplus country was generally left untouched.

It is difficult, however, to expect such multilateral 'aid' agencies to bring about realignment between the economic position of the dominant industrialised countries which exerted a major influence over their policies, and the developing countries which are in need of assistance. One reason is that both the IMF and World Bank rely for their resources upon the surpluses generated by the surplus countries, and therefore cannot help but adopt the 'free trade' ideology which has been the natural viewpoint of the dominant countries in international trade.

As the 'Economic Declaration' at the 1979 Non Aligned Summit, in Havana, (quoted earlier) stated more strongly "much of the disequilibrium in the developing countries' balance of payments was due to factors external to these countries, arising from fundamental maladjustments and inequities prevailing in the present world economic structures. Owing to the structure of the international monetary system, the burden of adjustment has fallen disproportionately on the developing countries with grave repercussions on their development programmes. These negative effects have been underscored and perpetuated by the strict conditionality and the rules as applied by the International Monetary Fund and other financial institutions which use these practices towards

developing countries having a deficit in their balance of payments."

The countries most seriously affected were the net oil-importing developing countries. They have been compelled to make strenuous efforts throughout the 1970's and early 80's to adjust to the deterioration in their external conditions brought about through world recessions and the continuing deterioration in their terms of trade. The exporters of manufactured goods, attempted to adjust to this situation by accelerating their growth in export volume. This process, which required an increasing supply of goods, was facilitated by the availability of capital in international capital markets which they continued to fall back on and the establishment within the international Monetary Fund of an oil facility.

Other countries, whose exports consisted mainly of primary commodities and were thus unable to accelerate export volume growth, availed themselves of international finance to maintain moderate growth in import volumes. In some cases a policy of import substitution was pursued with a certain degree of success, but in others the necessary adjustment was only postponed. The current economic crisis, which began in 1979, has involved most developing countries in significant losses in their terms of trade and greatly reduced their short-term prospects for an expansion in export volumes.

Increased balance of payments pressures narrowed the policy options available to governments in 1979 and 1980, many of which were also concerned with the acceleration of inflation due in large part to the rapid increases in the prices of imports of fuel and manufactured goods. Consequently, many developing countries were left with no option but to alter their economic policies by placing greater emphasis on measures to reduce demand rather than on efforts to increase supply. The result has been a marked reduction in GDP growth during the three year period 1980-1982 as compared with the period 1975-1980. Official statistics reveal that in 1981 the growth performance of oil-importing developing countries was the worst in the post war period.

The widespread nature of the economic crisis facing developing countries is illustrated by the large number of countries which have taken deliberately restrictive policy measures to reduce internal demand. For example, it has been observed that 15 among 25 developing countries (for which data for the years 1980 and 1981 was analysed in an UNCTAD study) reduced the amount of fiscal stimulus provided by the public sector in at

least one of these years despite the fact of falling or negative GDP growth rates in 70 percent of the cases. In nearly all cases the reduction in stimulus took the form of expenditure reductions rather than increased revenues, which has meant reductions in public investment programmes.

The global recession has contributed greatly to current difficulties. Between 1980 and 1982 falling export income and rising debt service have together had a negative impact of about \$ 70 billion on the balance of payments of the developing countries. For the oil-importing developing countries, the ratio between the payments on medium and long-term debt and export income jumped from 18 percent in 1980 to 24 percent in 1982. The ratio between debt outstanding and exports jumped, too from 1:1 to 1:3.

The top 20 borrowers are responsible for three-fourths of all Third World debt, and for them the ratio between payments on medium and long-term debt and export income has climbed from 26 percent in 1980 to 34 percent in 1982. It was even worse for the four biggest borrowers who had to delay repayments and all faced payments on medium and long-term debt that exceeded 50 percent of their export income in 1982.

The sudden increase in level of debt service ratios can be traced primarily to the world recession of the early 80's. The export sales of the developing countries were virtually stagnant in 1982; while terms of trade and export prices, have deteriorated for most developing countries, making the real burden of their debt even greater. The low income countries have been particularly affected by the fall in commodity prices. These nations suffered a 30 percent drop in their terms of trade between 1979 and 1982.

About half the increase in Third World debt service payments since 1980 has also been due to higher interest rates. Real rates of interest averaged 2 percent in the Sixties, were negative in the mid-Seventies, but then jumped to 5 percent by 1981. Although nominal interest rates declined, real rates are still high by historical standards, especially for countries whose exports are not rising. The main cause of high interest rates has been the combination of anti-inflationary monetary policies and burgeoning budget deficits in the industrial countries. A one point increase in interest rates cost Mexico, Brazil and Argentina \$ 1.2 billion a year.

Trapped in Debt

The "Debt Trap" into which developing country borrowers, both big and small have fallen is strongly depicted in a recent report of the World Bank on the debt situation as at the end of 1983. Poor

countries are paying back more than they are getting in loans, reversing a long term trend; while the thirteen biggest borrowers repaid \$ 21 billion more than they took in 1983. Equally depressing was the fact that when a country made a payment on its debt, interest due (on average) was almost half of it.

In its latest tabulation the World Bank shows that in 1983 all poor countries paid out \$ 11 billion in repayments and interest more than they received. In 1982, the flow went the other way: Loans to poor countries exceeded repayments by \$ 6.6 billion while in 1978, that figure was \$ 32.8 billion.

The report adds that money lent to the poor countries - a high proportion of the World Bank's 146 members - creates more goods, jobs and a higher standard of living when it was well used and not siphoned off into bribes and graft. But, when the poor countries pay back more than they get in new loans, growth rates slow down in manufactures, food supplies, and jobs so that the country grows even poorer.

In the last two years, living standards have dropped in nearly all of Latin America. The average Southern African has less food available than immediately after World War 11.

"..... The financial system withstood the strain in 1983, but the growth of the developing countries was slower than in any year since World War 11", the report said.

The increased debt burden also means bad news for richer countries. The poor countries tightened their belts to get money for repayments at the expense of industrial nations.

"Falling exports to developing countries constitute a threat to the vigour of recovery in the industrial economies" the Bank said.

According to the World Bank's figures, the 13 biggest borrowers repaid \$ 21 billion more in 1983 than they took. Each of these countries owed more than \$ 13.5 billion at the end of 1982. They are, in alphabetical order: Algeria, Argentina, Brazil, Chile, Egypt, India, Indonesia, Israel, South Korea, Mexico, Turkey, Venezuela and Yugoslavia.

Brazil and Mexico are the biggest, with Brazil's debt soaring close to \$ 100 billion. The total debt from the 13 countries totalled \$ 810 billion at the end of 1983, up from \$ 766 billion at the end of 1982.

The increase appeared to be due largely to rising interest costs. In 1983, when a country made a payment on its debt, the interest on average, amounted to almost half, \$ 46,000 million out of a total \$ 96,000 million.