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DEBT AND THE THIRD WORLD

Introduction

In the last year the governments of five developed countries (dcs) including Britain have cancelled some of the debt owed to them by the poorest less developed countries (ldcs). Similar action is being considered by other dcs, following a ministerial meeting of the United Nations Conference on Trade and Development (UNCTAD) in March this year. Discussions on the remaining external debt of the Third World will be held at the UNCTAD V meeting in Manila in 1979.

The purpose of this briefing paper is to consider how far the increasing amounts of loans (and their hardening terms) have created external debts of such magnitude that they have become a problem. The first part of the paper considers how the ldc debt issue has become the subject of international negotiation, the second part examines the case for generalised debt relief by considering the dimensions of ldc debt in detail, and finally the third and fourth parts examine the specific proposals put forward at the recent UNCTAD meeting on *oda* debt relief for the poorest and methods of handling the commercial debt problems of the higher income ldcs.

There are four major sources of finance available for the development of less-developed countries: domestic production (which may be converted into foreign exchange via the export market); private foreign investment; foreign commercial finance; and foreign concessional finance (soft loans or grants). Concessional finance from governments which is intended for the welfare of the recipient countries is known as official development assistance (*oda*). In recent years many developing countries have had to face higher import prices – especially for oil and manufactures – fluctuating export earnings, and slow-growing or stagnant *oda* receipts, and for a variety of reasons many have failed to attract significant direct foreign investment. A number have therefore resorted to large-scale foreign commercial borrowing in order to sustain development programmes or simply to avoid severe austerity.

The debt issue in North-South relations

The treatment of ldc debt as a special problem dates from as early as 1960, when the World Bank published some of its first statistics on ldc debt, showing the debt service payments of certain Latin American countries to be absorbing a significant share of their export earnings. By 1965 the OECD Development Assistance Committee (DAC) had recommended that all *oda* loans to ldcs should be on soft terms, partly to avoid the creation of a repayments problem, and donors were encouraged to give aid on softer terms to ldcs with large debts. Subsequently it was realised that the distribution of aid in this way would reflect past borrowing patterns rather than current needs. In addition donors began to emphasise that loans should only be made for projects where the returns would exceed the cost of borrowing. But this approach became difficult to enforce as loans were made increasingly to ldcs to solve balance of payments problems rather than to finance projects with specific returns. In 1968 at UNCTAD II, a resolution was passed initiating a comparative study of payments on private and public loans. In 1972 the debt question was referred to another UN experts group following ldc suggestions that general guidelines be drawn up to deal with the relief of both official and commercial debts of all ldcs, as necessary.

Concern about the balance of payments difficulties of non-oil ldcs increased with the oil price rise in 1973 and the beginning of the economic recession in 1974. In their proposals for a new international economic order the ldcs as the Group of 77† included demands for general debt moratoria, though some ldcs wanted to restrict these to *oda* debts. In early 1976 at a preparatory meeting for UNCTAD IV in the Philippines, they issued what is now known as the Manila Declaration. This called for several measures to be taken by dcs and international organisations, such as the World Bank, to resolve and alleviate what the Declaration termed 'the critical debt problem of developing countries'.

(1) With regard to debts arising from *oda* loans, the Group of 77 proposed that bilateral donors should provide relief, in the form of waivers or postponement of interest payments and/or cancellation of principal repayments, to any ldcs seeking such relief. In the case of the 29 least developed ldcs (lldcs)† it recommended that cancellation of *oda* debt, while for the 45 most seriously affected ldcs (MSAs)†, which include most lldcs, it suggested the same treatment or, as a minimum,

* The Institute is limited by guarantee.

† See Appendix

the postponement of *oda* service payments until these countries were no longer classified by the UN as MSAs. As for other concessional debt owed to multilateral development finance institutions, such as the World Bank or the Asian Development Bank, the Group asked these organisations for an increase in their assistance to each ldc at least equal to the debt service payments being received from them.

(2) With regard to commercial debts, the ldcs called for consolidation and the rescheduling of payments over a period of at least 25 years, for any interested ldc. This would require the establishment of financial machinery such as a multilateral facility to fund the short-term debts of interested ldcs.

(3) The declaration called for a conference of debtors and creditors to be convened under UNCTAD in 1976, to determine appropriate ways of implementing these principles and guidelines on the renegotiation of official and commercial debts.

At the UNCTAD IV Conference, held in Nairobi in 1976, although debt was listed as a major issue, no agreement was reached between ldcs and dcs on any of the points raised in the Manila Declaration. The dcs of Group B* felt that although certain ldcs faced substantial balance of payments problems as a result of their debt obligations, ldc debt did not pose a problem to which general solutions were appropriate. In particular, they were unwilling to agree to general measures on commercial debt and there was some congruence of view between them and some of the richer ldcs which were concerned about the impact of such measures on their overall credit-worthiness. As in the past, Group B were prepared only to consider debt relief, for *oda* debt, on a case-by-case basis. There was a feeling that existing mechanisms were adequate: debt relief, in the form of rescheduling, had been organised in the past for nine countries, including Zaire and Brazil. They saw the debt problem as only one element in the more general question of the transfer of resources to ldcs. The Socialist bloc, Group D, while recognising ldc debt as a problem, felt this was part of the colonial heritage for which they were not responsible.

It was not until the final session of the Conference on International Economic Cooperation, in May 1977, that some progress was made in the international debate on ldc debt when the eight representatives of the Western industrial countries agreed to set up a $1 bn[1] 'special action fund' to be channelled to low-income ldcs facing balance of payments problems. As its contribution to this fund, Canada cancelled the $254m *oda* debt owed to it by lldcs. This move was followed by the Netherlands as a result of a decision taken in 1975, and later Sweden, which also cancelled the debts owed to them by the lldcs (and MSAs in the case of Sweden bringing the total to some $200m) while Switzerland cancelled the $50m debts owed to it by six ldcs with annual per capita incomes in 1976 of less than $560. But there remained differences in the Group B and the Group of 77 proposals. The EEC countries together with the USA proposed setting up mechanisms to handle defaults, as they occurred, on concessional and commercial debts. They suggested these be dealt with separately, the first in aid consortia and the second in creditor clubs, a distinction not accepted by the Group of 77. Furthermore the ldcs wanted debt relief flows to be linked to internationally agreed development objectives.

In the meantime the Group of 77 have moderated their demands. Although they have never asked for general debt relief, they have suggested it in three cases:

(1) all lldcs;
(2) all MSAs;
(3) all other ldcs who want it.

By the end of 1977 it became clear that the Group was prepared to reduce its demands to writing off both the commercial and concessional debt of the countries in the lldcs alone; in particular it argued that it was inconsistent for countries in receipt of grants to continue to make repayments on former *oda* loans. More moderate forms of relief were proposed in the second case. At most they were asking for $20bn, or less than 10% of the total ldc debt of $250bn, to be written off. It was hoped that the Group B countries would accept these proposals to help the most needy as an extension of the 'case-by-case' principle, which they supported, rather than of the 'generalised', which they denounced.

In the second week of March 1978 a conference of the developed and developing countries was held under the auspices of UNCTAD to negotiate these issues. The meeting itself appears to have stimulated changes in some donor countries' attitudes. Judith Hart, UK Minister for Overseas Development, spoke of 'significant evolution' in UK government thinking on the inconsistency between giving grants to the poorest ldcs* and expecting them to repay old loans. Two major decisions were taken:

> (1) donor countries agreed to consider adjusting the terms of past *oda* debt of many poorer ldcs, particularly the lldcs among them, to bring them into line with current terms of *oda*; and,
>
> (2) it was agreed that an inter-governmental group of experts would draft a code for the handling of debt problems of individual ldcs by UNCTAD V, to be held in 1979.

However, even these results have had a mixed reception. The Secretary General of UNCTAD, Gamani Corea, as well as the Group B representatives, declared the conference to have been a breakthrough in the North-South dialogue. Some ldcs, including Tanzania and Iraq, were less enthusiastic. In particular they were concerned that there was no general and binding commitment to cancel the *oda* debt of all the poorest ldcs. In fact Britain has recently announced a decision to write off the $1.7bn *oda* debt owed by 17 of the poorest ldcs. But there is some doubt as to how many other dcs will be prepared to follow suit. Another source of disappointment was the lack of progress on the issue of lldc commercial debts; there was agreement on the need for a code to handle the debt of individual ldcs in balance of payments difficulties, but there was no explicit reference to commercial debt.

The dimensions of ldc debt

There are two reasons for recent concern with ldc debt: its growing size and the increasing element of commer-

* See Appendix.

[1] 1 billion = 1,000 million.

cial debt which together have contributed to rising debt service payments.

(1) *Size*. Latest figures suggest the outstanding debt of ldcs had risen above $250bn by the end of 1977, from $73bn at the end of 1970, showing an average annual increase of 19%. In real terms, however, the increase has been less substantial. Using an export price index[1] as a deflator, the real debt has risen $37bn in seven years, to $110bn, at an annual average rate of 6%[2]. Nor is it meaningful to talk in aggregate terms as the level of debt varies significantly between different groups of ldcs and even within these groups. At the end of 1976 (the latest year for which a breakdown of debt by groups of ldcs is available – compiled by DAC[3]) the total disbursed debt of all ldcs was $207bn. This figure covers 140 ldcs including 13 OPEC countries. Table 1 shows that the group of ldcs with the largest debt is that of the non-oil ldcs with incomes greater than $265 per capita per annum, which accounted for 68% of the total ldc debt, while the OPEC countries accounted for only 17%. All three groups experienced differing nominal growth rates in their debts over this period: the highest being in the case of the 'other non-oil ldcs' at 21% average per annum, followed by OPEC at 20%, while the debt of the 37 poorest ldcs grew more slowly at only 13%. The debt of this last group rose by a mere $300m in real terms[4] over this period. Within each group, debt is highly concentrated. This is particularly true of the poorest ldcs' debts, $17.2bn (62%) of which was attributable to India and Pakistan (in 1975),[5] while in the richer non-oil ldcs, eight countries, Argentina, Brazil, Egypt, Israel, Korea, Mexico, Spain, and Yugoslavia, accounted for 57% or $66.3bn(also in 1975). Amongst OPEC, Algeria and Indonesia shared 56% or $16.0bn of this group's debt.

(2) *Type*. These figures include debt incurred by ldc governments or public institutions on concessional terms as a result of bilateral and multilateral aid; on commercial terms, ie other official flows (mainly official export credits); officially guaranteed private export credits *as well as* estimates of debt owed by the ldcs' private sector which has not been officially guaranteed; and inter-ldc loans. They exclude debt to the IMF, short-term and military debt, as well as foreign claims by ldc governments or individuals, ie finance owed to them. Underlying the growth in total ldc debt there has been a significant shift away from loans on concessional terms to loans on commercial terms. The following table shows that nearly 80% of the $134bn increase in ldc debt since 1970 has been incurred on commercial terms, raising the share of commercial debt in the total outstanding from 61% in 1970 to 73% in 1976. Conversely, the relative importance of loans on concessional terms has fallen to a fifth of all new debt since 1970.

Table 1. Total disbursed debt at year-end by group of developing countries ($bn)

	1970	*1971*	*1972*	*1973*	*1974*	*1975*	*1976*
Poorest ldcs[a]	15.0	16.8	18.6	21.1	23.7	27.7	31.4
Other non-oil ldcs	46.2	52.0	57.6	68.9	89.1	116.4	140.8
OPEC	11.7	14.5	16.7	22.4	24.4	28.8	34.6
Total	72.9	83.3	92.9	112.4	137.2	172.9	206.8

[a] for definitions see Appendix. Source: OECD, *1977 Review, Development Co-operation*, Paris, 1977, p214.

Table 2. Total disbursed debt of developing countries at year-end by type of debt ($bn)

	1960	*1970*	*1971*	*1972*	*1973*	*1974*	*1975*	*1976*[a]
Concessional	5.4	28.7	31.0	33.5	38.0	42.8	51.5	56.8
Commercial	12.5	44.2	52.3	59.4	74.4	94.4	121.4	150.0
(of which:								
export credits	7.2	26.0	29.9	31.4	34.3	38.9	49.3	61.5
other	5.3	18.2	22.4	28.0	40.1	55.5	72.1	88.5)
Total	17.9	72.9	83.3	92.9	112.4	137.2	172.9	206.8

[a] Provisional figures. Source: OECD, *op cit* p213.

1 The indexed export price of non-fuel primary commodities, if 1970 = 100, in 1977 = 228 (GATT Press Release, 9 March 1978).

2 All growth rates are expressed in compound terms.

3 OECD, *1977 Review, Development Co-operation*, Paris, 1977.

4 The indexed export price of non-fuel primary commodities in 1976 = 205.

5 Source: OECD, op cit p29.

There are several possible explanations for this changing structure. First, following a trend towards softer aid policies donor countries are increasing the volume of grants to ldcs whilst running down the volume of loans. Second, it can be argued that the growth of total *oda* transfers (ie both loans and grants) has been unable to meet the growth in demand by ldcs for resources to finance their development. Third, sources of commercial finance, in particular private banks, increased their loans to ldcs from 1973 when they found themselves liquid with 'surplus' OPEC funds yet facing a shortage of demand from traditional borrowers in dcs. Finally, dcs have themselves used export credits as a means of raising the effective demand of ldcs for dc exports. Outstanding export credits at the end of 1976 were more than twice as large as those at the end of 1970.

While on aggregate there has been a shift to seeking loans from commercial sources, the borrowing patterns of different ldcs have varied significantly. However it is suggested that within each income group of ldcs there is some consistent behaviour.

Table 3 shows that for the poorest ldcs the bulk of their loans (55%) are on concessional terms. It is interesting, however, to note this proportion has decreased substantially from 1970 when it was 81%. For the richer ldcs, commercial sources have always been more important than concessional ones. This importance has been growing for the ldcs with annual per capita incomes above $520, and for OPEC, to the point where almost all their loans are on commercial terms. In fact, two higher income ldcs*, Brazil and Mexico, account for over half ldc debt to commercial banks. In the case of the middle income ldcs*, concessional loans are now of increasing importance. Within each group, of course, there are further differences. For example, commercial loans are no longer a net source of finance for India: in 1975 repayments more than offset new loans, whereas in Tanzania commercial loans (net of repayments) amounted to 20% of total loans obtained in that year.

(3) *Debt service: A problem*? Associated with the growing debt of ldcs is a steady rise in amortisation and interest payments necessary to service this debt. This trend has been accentuated by the increasingly hard terms of the commercial loans. Debt service on concessional and commercial loans outstanding rose 2.9 times between 1970 and 1975 while total debt rose 2.4 times. Table 4 shows that for all ldcs an increasing share of new loans is necessary to repay old loans. The situation varies considerably between all groups of ldcs. Whether the large volume of debt service constitutes a problem, let alone a growing one, obviously depends on the circumstances of each ldc. The obligation to pay debt service before loans or foreign exchange earnings can be used to finance development may appear to be a problem. But, provided an ldc can use a loan sufficiently

Table 3. Loans by type and by income group ($bn)

	Poorest ldcs[a]	*Middle income ldcs*	*Higher income ldcs*	*OPEC*[b]
1970				
Total[c]	1.82	1.27	5.82	1.01
Concessional[d]	1.48	0.24	0.98	0.06
Commercial	0.34	1.03	4.84	0.95
1975				
Total	5.58	3.33	13.34	2.89
Concessional	3.08	0.94	1.04	0.09
Commercial	2.50	2.39	12.30	2.80
Change 1975 on 1970				
Total	3.76	2.06	7.52	1.88
%	207	162	129	186
Concessional	1.60	0.70	0.06	0.03
%	108	292	6	50
Commercial	2.16	1.36	7.46	1.85
%	635	132	154	195

[a] See Appendix for definitions.
[b] excluding Nigeria and Indonesia.
[c] Total = total flows net of repayments less total grants.
[d] concessional = *oda* loans net of repayments.

Source: derived from OECD, *Geographical Distribution of Financial Flows to Developing Countries*, Paris, 1977, pp270-83.

* See Appendix

productively to generate the foreign exchange necessary to service it, and provided there is no offsetting deterioration in its balance of payments from other causes, no debt problems will arise. One of the criteria most widely used (especially by banks) for measuring the ability of a ldc to finance its debts is the ratio of debt service to export earnings, known as the debt service ratio. Although unsatisfactory as an indicator of a country's creditworthiness or as an early warning of an impending debt crisis, it can be used to indicate the degree of short-term rigidities in a country's balance of payments. As can be seen in Table 4, this has actually fallen for ldcs on aggregate – though not substantially. But for the low income ldcs the debt service ratio has risen and one fifth of export earnings was necessary to repay debts in 1975. More important, the level of the debt service ratio is likely to rise between 1978 and 1980 as repayments on many commercial loans with hard terms fall due in this period, while ldcs are unlikely to be able to greatly increase their foreign exchange earnings because of the world recession. Within each group, however, some countries have to devote between a third and a half of their export earnings to service their debt. Amongst the higher income ldcs, these figures in 1975 were as high as 40% for Brazil, 34% for Mexico, 28% for Argentina, and 27% for Peru, and it is estimated that if repayments on private debts are included they will bring the ratio to more than half in the case of Brazil (*Guardian* 9/3/78). Among the poorest countries, Afghanistan has to commit nearly 30% of its annual foreign exchange earnings to meet the service on its $1bn debt (UNCTAD Press Release 9/3/78). Even where the ratio is much lower, there may be a problem for the poorest ldcs in that the resources for development are scarce and any loan repayments are a drain on these resources.

Despite the similarity in debt service ratios of these various groups of ldcs, it is argued that having external debts presents very different problems for each group. What these differences are and how far the decisions taken at the UNCTAD meeting in March cope with them will now be discussed.

Debt relief for the poorest

The previous section has shown that the debt of low income ldcs has only increased by 2% in real terms since 1970 while as a proportion of total ldc debt it has fallen from 21% to 15%. One reason for this is that these countries have been too poor to attract commercial loans. Another reason is that donor countries have been increasing the proportion of grants in their aid to the poorest ldcs. In 1975 the UK government announced, in its White Paper[1], that all future aid to the poorest ldcs would normally be in grant form. DAC recommendations for terms of aid, introduced in 1972, have been limited to the smaller group of lldcs for whom they suggested aid should preferably be in the form of grants. In 1975 the grant element of DAC members to the 29 lldcs averaged 91.6%. Some countries have already decided to give all new aid to lldcs in grant form: Sweden (from 1974), Finland (from 1976), Australia, New Zealand, Austria, and the Netherlands (from 1977). By the time of the March 1978 meeting on debt it had become clear to most donor countries that receiving *oda* loan repayments from the poorest ldcs was inconsistent with these new aid policies. They agreed, therefore, to consider adjusting the terms of past *oda* debts of the poorest ldcs to fit in with current aid terms. It is necessary to underline that they did this not in the belief that indebtedness was a problem per se, but in the more general context of the need to increase resource transfers for the poorest countries.

Table 4. Debt service by group of ldcs ($bn)

	Poorest ldcs	*Middle income ldcs*	*Higher income ldcs*	*OPEC*	*Total*
1970					
(1) Debt service	1.0	7.0		1.0	9.0
(2) Outstanding debt (disbursed)	15.0	46.2		11.7	72.9
(1)/(2) as %	7	15		9	12
(3) Exports	6.0	38.1		17.6	61.6
(1)/(3) as %	17	18		6	15
1975					
(1) Debt service	2.1	2.5	16.3	5.2	26.0
(2) Outstanding debt (disbursed)	27.7	19.8	96.8	28.8	172.9
(1)/(2) as %	8	13	17	18	15
(3) Exports	10.5	14.4	88.2	109.7	222.8
(1)/(3) as %	20	17	19	5	12

Source: OECD, *1977 Review, Development Co-operation*, Paris, 1977 p210, p214, and OECD, *Geographical Distribution of Financial Flows to Developing Countries*, Paris, 1977.

[1] HMSO *The Changing Emphasis in British Aid Policies: More Help for the Poorest*, London, 1975, Cmnd 6270.

What will be the impact if consideration leads to a favourable decision? There are a number of questions requiring clarification. *First*, which ldcs will benefit? The use of the term 'poorest' has been imprecise. The Group of 77 originally demanded debt cancellation for the 29 lldcs. Since then discussion on *oda* debt relief has included the other 21 MSAs and occasionally the other 5 ldcs with per capita GNP of $265 or less. The cost of debt relief will increase as the definition of the target group is expanded; the total outstanding *oda* debt of the 29 lldcs is $2.2bn with annual debt service of $69m; of the other 21 MSAs it is $13.1bn with annual debt service of $510m; and of the other 5 poorest ldcs it is $3.5bn with annual debt service of $99m (see Table 5). In fact it has been left to each donor country to decide which ldcs need relief.

Second, what is meant by ex-post adjustment of terms? The ldcs wanted debt cancellation. But the resolution adopted in Geneva stated that donors could adjust terms or provide equivalent measures. Various forms of debt relief are being considered by different donors to find one whose implementation would face the least legal and institutional obstacles within the donor country. For example, the Japanese feel it would be easier to increase their aid to the poorest by amounts equal to the loan repayments owed by them than to cancel this debt outright, as such action would present legal difficulties. The impact on the ldcs in question would be the same as long as this aid was additional and untied. The Canadian exercise involved the conversion of loans to grants as they fell due. In effect the debts of 10 ldcs were written off but the cost to the Canadian aid budget was spread over time reducing it to $35m, the equivalent of 3% of the current aid budget in terms of present value[1], as compared with $254m, or 22% of the aid budget, had it been cancelled at once. Another possibility is that only a certain percentage of loan repayments will be cancelled – according to the percentage of aid currently being given in grant form.

Table 5. Outstanding debt[a] and debt service[b] of various groups of ldcs ($m)

A. Outstanding debt and debt service of the 29 lldcs

	Debt outstanding (disbursed)		*Debt service*	
	Total	*DAC/ODA*	*Total*	*DAC/ODA*
Afghanistan	787	158	23	9
Bangladesh	1622	671	70	3
Benin	99	28	9	1
Bhutan	0	0	0	0
Botswana	263	81	20	1
Burundi	15	2	2	0
Central African Empire	92	40	11	2
Chad	70	14	6	1
Ethiopia	387	156	32	5
Gambia	14	9	0	0
Guinea	211	123	24	9
Haiti	62	3	6	0
Laos	25	20	2	1
Lesotho	13	1	0	0
Malawi	262	144	17	5
Maldives	1	1	0	0
Mali	327	30	6	2
Nepal	37	15	5	1
Niger	114	76	13	4
Rwanda	22	2	1	0
Sikkim	na	na	na	na
Somalia	257	38	5	2
Sudan	1191	116	158	8
Tanzania	839	309	38	9
Uganda	209	86	29	2
Upper Volta	63	29	8	3
W. Samoa	16	0	1	0
Yemen Arab Republic	243	52	17	1
Yemen People's Republic	101	11	4	0
Total	7,342	2,215	507	69

1 ie the value of future repayments discounted to the present, calculated as (1 – grant element) x (debt held).

B. Outstanding debt and debt service of the other 21 MSAs ($m)

	Debt outstanding (disbursed)		*Debt service*	
	Total	*DAC/ODA*	*Total*	*DAC/ODA*
Burma	279	133	34	6
Cameroon	413	132	47	15
Cape Verde Islands	0	0	0	0
Egypt	5,135	571	532	34
El Salvador	268	53	70	3
Ghana	742	361	53	25
Guatemala	207	60	22	2
Guinea-Bissau	0	0	0	0
Guyana	261	107	26	7
Honduras	278	51	20	1
India	11,766	7,274	860	283
Ivory Coast	984	168	140	17
Kampuchea	31	25	2	0
Kenya	626	287	93	20
Madagascar	180	74	21	10
Mauritania	173	30	35	5
Mozambique	38	0	20	0
Pakistan	5,459	3,268	293	52
Senegal	294	80	44	9
Sierra Leone	182	48	21	4
Sri Lanka	620	334	129	17
Total	27,936	13,056	2,462	510

C. Outstanding debt and debt service of the 5 remaining poorest ldcs ($m)

	Debt outstanding (disbursed)		*Debt service*	
	Total	*DAC/ODA*	*Total*	*DAC/ODA*
Comoro Islands	5	5	1	0
Indonesia	8,917	3,207	596	90
Timor	0	0	0	0
Viet Nam	209	164	7	2
Zaire	2,233	146	213	7
Total	11,364	3,522	817	99

NB na not available
0 negligible
[a] at end of 1975
[b] in 1975

Source: derived from OECD, *1977 Review, Development Co-operation*, Paris, 1977, pp208-9.

A major worry is that the aid involved in any of these relief exercises will not be additional *either* to that already being received by lldcs *or* to total aid programmes. If the $2.2bn of *oda* debt owed by lldcs were cancelled immediately, this would cost the equivalent of 14% of total DAC *oda* (gross) in 1976 but only 0.0054% of their combined GNP. What action, and for what ldcs, individual donors finally decide to take will vary according to the cost and the legal and institutional context of their aid programmes. For Britain, which is owed $1.7bn by 17 of the poorest ldcs with annual service payments of $116m, cancellation of loans as they fall due will cost the equivalent of 14% of net *oda* in 1976 – while in the case of the US, debt cancellation for the poorest ldcs would mean foregoing repayments of $1077m in 1976 equal to 32% of the aid budget. Thus at present it seems likely, in view of budgetary constraints, that *oda* debt relief will be given as a substitute for some of the current *oda*, rather than additional to it.

Perhaps a more serious problem is that of the remaining non-bilateral *oda* debt, largely commercial, which constitutes 70% of outstanding (and disbursed) debt of lldcs, and 53% of the other MSAs debt (see Table 5), and which accounts for an even larger share of debt service payments.

Guidelines for future debt problems

While the Group B countries have denied the existence of a general debt problem, they have accepted the need for setting up multilateral procedures to handle individual cases, as proposed by the EEC and the US in 1977. The Group of 77 would like to see a new institution established to deal with these problems. In particular such procedures would deal with cases of debt mismanagement – where ldcs face bunching of loan repayments and, as a result, serious (but temporary) balance of payments difficulties[1] – as well as a case of poor risk assessment. The procedures proposed would allow the meeting of a debtor ldc with its commercial and other creditors to discuss appropriate debt relief. Exactly what form this would take is not yet known but there are two options; in the case of the short-term crises which occur in ldcs dependent on commercial debt, rescheduling may be necessary, while in the case of ldcs with longer term structural problems, more assistance on concessional terms may be appropriate as well as debt cancellation. Whichever is chosen, it will mean that creditors are increasingly drawn into the economic management of debtor countries.

[1] In 1977, Witteveen, the managing director of the IMF, proposed a new fund of $10bn to be lent to countries with balance-of-payments difficulties. The future of the fund now depends on Congress confirming the US contribution.

Finally, it should be stressed that although individual ldcs may face acute debt problems as a result of economic mismanagement on their part, such problems may also arise as a result of factors beyond their control, such as worsening terms of trade, which put pressure on their balance of payments as a whole. In addition, their difficulties may be exacerbated as a result of protectionism in developed countries, which denies them opportunities to earn foreign exchange.

Appendix

29 least developed countries (lldcs) – those which satisfy at least two of the following criteria:

(1) per capita gdp of $100 in 1968 ($125 in 1970-2) or less;
(2) share of manufacturing in gdp of 10% or less;
(3) literacy rate (proportion of literate persons in the age group of 15 years and above) of 20% or less.

45 most seriously affected countries (MSAs) – those countries with per capita incomes in 1972 of less than $400 which were most affected by recent economic developments, in the sense that they had, on average, a projected balance of payments deficit for 1974 and 1975 not smaller than 5% of imports. These include 24 of the lldcs. Both these definitions were officially introduced by the UN, the first in October 1971, the second in May 1974.

Poorest ldcs – those with annual per capita incomes in 1975 of less than $265.

Middle income ldcs – those with annual per capita incomes in 1975 of $266 to $520.

Higher income ldcs – those with annual per capita incomes in 1975 of more than $520.

Group of 77 – the ldc members of UNCTAD – originally numbering 77, now 114.

Group B – the 'Western' industrial members of UNCTAD, including Australia and Japan.

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