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Multilateral Debt Burden

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Multilateral debt is that portion of a country's external debt burden owed to international financial institutions (IFIs) such as the International Monetary Fund (IMF) and the World Bank. For most of the world's most impoverished countries, multilateral debt looms larger than other debts because the IFIs provide low-interest balance-of-payments loans, giving them "preferred creditor" status. This status means that payments to them must be given the highest priority, over private and bilateral (government-to-government) debt. These institutions also maintain that their bylaws prohibit them from granting debt relief or writing off debts, as governmental and private creditors often do. Debtor governments have a special incentive to stay current with their multilateral debts, since IFIs determine the creditworthiness of countries: Until the IMF gives its stamp of approval, which requires adherence to the economic policies it stipulates, impoverished countries generally cannot get credit or capital from other sources. Until a country has signed onto an IMF program, it cannot apply for bilateral debt relief from the "Paris Club" of creditor countries.

Key Points

- In 1996, sub-Saharan Africa paid $2.5 billion more in debt servicing than it received in new long-term loans and credits.
- The IMF and the World Bank are "preferred creditors" who gain power over impoverished countries as the amounts owed to them increase.
- Structural adjustment programs, which reorient economies to benefit corporate interests while reducing spending on social programs and locally oriented production, are imposed by IFIs on severely indebted countries.

Significant growth of multilateral debt began with the Latin American debt crisis of the early 1980s. Mexico, Argentina, and Brazil all came to the brink of defaulting on loans that large private banks had freely offered during the 1970s to developing country governments in Latin America and elsewhere. The IMF and the World Bank responded with massive loan packages conditioned on implementation of structural adjustment programs (SAPs), packages of neoliberal economic reforms designed to restore economic health to indebted countries. With this move, both institutions were changing course: The IMF was shifting from short-term, balance-of-payments loans mainly for industrialized countries to medium-term loans for developing nations, and the World Bank was adding policy-linked loans to its infrastructure development projects. Private debts were converted into multilateral debt as countries used the funds acquired from the IFIs to pay off banks that would no longer loan to them.

Multilateral debt is a problem for the entire global South, but it's particularly acute for the most impoverished countries. For low-income countries (defined by the World Bank as those with per capita GNP below $785), multilateral debt increased by some 544% between 1980 and 1997, from $24.1 billion to $155.3 billion, and currently constitutes 32.75% of their total long-term debt burden (versus about 25% in 1980). For the most severely indebted of those low-income countries, multilateral debt increased by 459%, from $10.6 billion to $59.3 billion, with a corresponding percentage increase in their long-term debt from 22.3% to 30%. During this same period, the debt burden of middle-income countries—those with per capita GNP between $785 and $9600—increased by 481%, amounting to a comparatively modest 15% of their total long-term obligations (up from 9.4% in 1980). In 1996, sub-Saharan Africa paid $2.5 billion more in debt servicing than it received in new long-term loans and credits.

The impact of debt is felt in two ways—through the diversion of national resources to debt servicing and through the effects of SAPs, which are designed to transform economies from production for the local market to a "globalized" model of production and export of whatever garners the most hard currency. SAP-linked IFI loans are meant to finance the redesign of governmental, industrial, and commercial systems to enable countries to continue to pay debt servicing. However, SAPs have almost invariably caused increased poverty, unemployment, and environmental destruction and have usually led to an increase in the overall size of a country's multilateral debt. The universal failure of the standard SAP recipe has meant that debt and structural adjustment simply end up fueling each other.

A global movement called Jubilee 2000, which calls for external debt cancellation for the poorest and most indebted countries, has gained great momentum. With national campaigns in some fifty countries (about half of them in the South) and the visible support of celebrities like Muhammad Ali and U2's lead vocalist Bono, the movement has put a scare into the IFIs. In response to Jubilee 2000, the G-7 countries suggested a somewhat-more-generous version of the IMF/World Bank debt management program at their June 1999 meeting in Cologne, Germany. Several G-7 countries, including the U.S., have indicated a willingness to cancel 100% of the bilateral debts owed them by the most impoverished countries—as long as the debtors adhere to structural adjustment programs.

Problems With Current U.S. Policy

Voting power at the World Bank and the IMF is apportioned according to the size of each country's monetary contribution. The U.S. has by far the largest share (18% of all votes) and can veto policy decisions, since they require an 85% vote. The IFIs may not be totally controlled by the U.S., but it's close: the *New York Times* recently described the IMF as a "proxy" of the U.S. government. Any analysis of IFI policies is thus also a critique of U.S. policies.

The response of the World Bank and the IMF to the debt crisis was the Heavily Indebted Poor Countries (HIPC) Initiative of 1996, revised in 1999. The ostensible aim of the program is to determine which countries have "unsustainable" burdens, then to caucus with each country's creditors to reduce the debt across the board until it is "sustainable." The program seeks to ensure that countries do not run up "unsustainable" debts again by insisting that beneficiaries demonstrate a proven commitment to "sound economic policies"—the IFIs' usual euphemism for SAPs.

To qualify for HIPC, a country must complete three years under an IMF-designed SAP. Even after that hurdle, the country must fulfill a further three years bound by another SAP before relief on multilateral debt is granted. At that time, all creditors will give matching relief to reduce the country's debt to a "sustainable" level. The new version of HIPC allows for the granting of relief as soon as the debtor country completes its first SAP, though the debt can be reinstated if the second SAP is not fulfilled to the IMF's satisfaction. The cruel paradox here is that countries in desperate need of debt relief so they can begin to direct resources to social sectors are required to first demonstrate their willingness to make things worse by depriving their people of health care, food subsidies, and education.

The new version of HIPC seeks to ensure that debt relief will effectively reduce poverty through the Poverty Reduction and Growth Facility (PRGF), the new name given in September 1999 to the IMF's Enhanced Structural Adjustment Facility (ESAF). The IMF claims that the new program relies on government and civil society to come up with their economic programs and that the primary goal of the programs will be poverty reduction. But civil society organizations in Uganda and Tanzania, two of the first countries to embark on the PRGF, report that the IMF still expects to provide the basic economic framework, with civil society filling in some details and signing off.

There are indications that the PRGF will simply become an additional stumbling block; for example, the U.S. government's dissatisfaction with Mozambique's and Uganda's Poverty Reduction Strategy Papers has delayed their debt relief packages. The PRGF is widely viewed as both a cynical public relations ploy and an expansion of the IMF's power, since, at Washington's insistence, the IMF now claims the right to oversee poverty programs.

There are other problems with HIPC's complex formulas. "Debt sustainability" basically means how much a country can repay without going broke. In many cases, countries are not paying all their debt-servicing bills because they simply haven't got the money. But the definition of "sustainability" is a harsh one: a debt-to-export ratio of 150%, meaning that a country's outstanding debt is one and a half times a large as annual exports. In practice, this means about 15% of a country's annual export income flows out of the country in the form of debt payments (capital plus interest).

Since the HIPC Initiative was adopted in 1996, only five countries—Uganda, Bolivia, Guyana, Mozambique, and Mauritania have received relief. And these countries have found HIPC relief to be worth relatively little. Uganda began to receive debt relief worth $350 million in April 1998, but, as a consequence, lost access to other debt relief funding mechanisms. With a drop in the international price of coffee, its chief export, Uganda found itself by April 1999 once again saddled with an officially "unsustainable" debt burden. Bolivia has been accorded a new HIPC deal, the first under the revised program; the promised supplements for Uganda, Mozambique, and Guyana have been delayed because of alleged failures to meet conditions.

Even under the new terms, Mauritania will continue paying as much on debt as on education, and Bolivia's payments will roughly equal its health expenditures. The meager results of the HIPC program suggest that its promises are hollow ones, made solely to ensure that countries remain on the debt and structural-adjustment treadmill when they might be tempted to default and opt out of the global financial system despite the prospect of losing access to markets and capital. The IFIs and the U.S. government also have incentives to avert defaults: any gaps in the globalized economy represent a loss of control and potential markets and may even end up evolving into an alternative model for economic development independent of U.S. influence.

Outright debt cancellation—the only humane solution to the most impoverished countries' debt crises—would undermine the policy leverage now exercised by the IFIs. The absence of debt burdens would make countries more creditworthy and thus less dependent on the IFIs' conditioned loans. In the wake of Hurricane Mitch's devastation in Central America, Treasury Department officials gave "loss of leverage" as their reason for refusing to consider comprehensive debt cancellation for Nicaragua and Honduras. President Clinton's September 1999 pledge of 100% forgiveness of bilateral debts owed the U.S. by the most impoverished countries was important for breaking that taboo. But it appears that his offer will be made only to countries graduating from HIPC and committed to ongoing structural adjustment.

Key Problems

- A voting structure determined by financial contributions means that impoverished countries have little voice in the IFIs, while the U.S. government holds nearly decisive power there.
- The more generous IMF/World Bank debt plan is still calculated less to provide meaningful relief than to ensure that countries continue to implement neoliberal economic policies.
- Maintaining leverage over other nations' economic policies is the central goal of U.S. Treasury policy on debt and the IFIs.

Toward a New Foreign Policy

For countries that have endured decades of severe indebtedness, poverty, and subordination to the IFIs' economic policies, comprehensive cancellation of their outstanding debts—without the added burden of crippling, externally imposed conditions—is necessary if their resources are ever to become available for development and if their people are ever to gain a sense of ownership of their economic destiny.

Key Recommendations

- Immediate and comprehensive debt cancellation is necessary for impoverished countries to function in the global economy on equitable terms.
- An international body—with strict requirements of fair representation, with an orientation to sustainable and equitable development, and with authority over the IMF and the World Bank—should be created for the adjudication of debt cancellation and reduction.
- Debts incurred for failed economic programs and nonperforming infrastructure projects should be annulled.

The U.S. government should ideally take the lead in such a program of cancellation, first by canceling the bilateral debt of the most impoverished countries without credit-imposed conditions, and then by strongly urging similar cancellation of multilateral debt. Even if that were to occur, a system for treating national debts independent of the IFIs is still necessary, particularly for the debts of countries like Brazil and Indonesia, which are not deemed to be among "the poorest" but which have huge populations living in abject poverty.

University of Vienna economist Kunibert Raffer has suggested a process for recognizing partial insolvency of national governments. Raffer cites provisions in U.S. law permitting debts of local governments to be treated like those of a company or an individual who has gone bankrupt, while guaranteeing that essential services provided by the municipality are not affected. Raffer maintains that this process could occur without the creation of a new international agency, and he suggests a panel of arbitrators with equal creditor/debtor representation. It is hard to imagine, however, that the World Bank and the IMF would have adequate incentive to participate without the creation of some new multilateral authority. The United Nations or World Court, for example, could consider establishing a body with authority over the IFIs and over creditor and debtor governments alike.

Once constituted, the new international bankruptcy body would function much like courts in the U.S. that adjudicate cases of insolvency or bankruptcy. It would be empowered to instruct creditors to accept a portion of their claims and demand no more, and it would establish a process for cleansing a country's credit record, so that nation could reenter the global economy on its own terms. This new entity would not have the power to insist on particular economic programs as a condition for debt reduction.

Objections to such a body are easy to imagine: the IFIs would fret that their status as preferred creditors would be threatened if decisions on debt relief were removed from their control. Such concerns should be met with the insistence—more easily imaginable, now, in the wake of the criticism IFI policies have received since the East Asian financial meltdown—that the IFIs must take some responsibility for the effects of the policies they have imposed around the world. If the lower interest rates charged by the IFIs have entitled them to special status, the harm done by the policies imposed with those rates must also be considered. In a similar vein, the World Bank should be pressured to annul debts owed to it for projects that its own analyses show to be economic failures. (A 1992 World Bank report, Effective Implementation, estimated 37.5% of World Bank projects should be so classified.) The proposed bankruptcy body should perform an assessment of which IFI claims are legitimate in light of their poor policy advice and failed projects.

The IFIs should also be forced to accept—through a change in their bylaws, if necessary—the option of writing off debts. Private banks do this routinely with loans they can never expect to be repaid, and many took some losses in resolving the Latin American debt crisis in the early 1980s.

Jubilee South, a coalition of Southern nongovernmental organizations involved in debt cancellation campaigns in Latin America, the Caribbean, Asia-Pacific, and Africa, calls for total cancellation of Southern debt without creditor-imposed conditions. They also demand an end to structural adjustment and the closure of institutions imposing neoliberal policies. Moreover, they insist on reparations and restitution for the damage done by debt, structural adjustment, and exploitative economic practices. The overriding imperative, at any rate, is a policy of extensive debt cancellation that avoids shackling debtor economies and compromising the sovereignty of debtor governments. The cancellation of multilateral debt must top the agenda of U.S. policymakers, whose influence within the IFIs is decisive.

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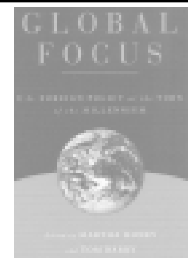

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