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**Mulford Pumps
Up The G7**

Next Stop: Caribbean Debt Relief?

by *Richard L. Bernal*

One of Jamaica's Key Economic Strategist Says "What's Good for Poland is Good for Us"

CURRENT ECONOMIC SITUATION AND OUTLOOK

At this time the Caribbean is at the most important crossroads in its history. It is faced with the serious dilemma of formulating and implementing a strategy to ensure development and avoid economic decline and social distress which can spawn crime, corruption and extremist political movements. The origins of this dilemma can be traced to the unprecedented disequilibrium in the balance of payments, caused primarily by adverse external events such as (1) the escalation in the price of oil during most of the 1970s and continuing into the 1980s, (2) the decline in demand for bauxite and traditional exports, and (3) natural disasters. Large and persistent deficits and the concomitant process of adjustment initially resulted in economic decline. This is evident in the low and fluctuating rates of economic growth

in the face of rapid population increase (1.3% per annum in 1970-80 and 1.4% since 1980) and persistent high unemployment (over 20% in Jamaica, Trinidad and Tobago, Guyana, St. Vincent, Grenada and St. Lucia).

The resuscitation of economic growth in the Caribbean is imperative if countries are to extricate themselves from the stifling economic deprivation which engulfs the majority of people and threatens the social stability and peace in which democracy can flourish. The vulnerability and fragility of democracies is evident in Haiti and in the recent attempted coup in Trinidad and Tobago, following the disastrous events in Grenada in the past decade. Furthermore, if the stranglehold of the debt burden on development is not broken, these societies could gradually become overwhelmed by widespread unemployment, increased crime levels, and other activities resulting from poverty.

The United States government is cognizant of this and has attempted to respond by launching the EAI (Enterprise for the Americas Initiative). The economic plight of the Caribbean has and will reflect itself in declining markets for U.S. exports, fewer investment opportunities, increasing susceptibility to involvement in drug trafficking, burgeoning migration, the necessity for increased development assistance and political instability. While U.S. exports to the region have expanded under the Caribbean Basin Initiative, this trend may be reversed because of a reduction in demand for U.S. goods and services.

ECONOMIC VULNERABILITY AND ADJUSTMENT

The process of economic growth is heavily dependent on imports and capital inflows in the case of small, open Caribbean economies. The volume of imports is, therefore, a principal determinant of the level of economic growth. Imports have to be paid for in foreign currency. The major sources of foreign exchange are: (1) export earnings, including tourism and (2) foreign capital inflows in the form of (a) foreign investments and/or (b) loans, either on commercial or concessionary terms. Traditionally, Caribbean economies have experienced adverse trade balance. However, the gap was financed by net inflows of foreign capital up to the mid-1970s, and therefore growth was sustained. During the mid 1970s, foreign investment in the bauxite/alumina industry, export agriculture and petroleum declined, reducing the

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ability to sustain an excess of imports over exports.

Since the late 1970s countries like Jamaica, Guyana, Trinidad and Tobago and the Dominican Republic have adhered to a series of IMF stabilization programs and World Bank adjustment programs to increase growth, reduce the balance of payments deficit, and control inflation. Due to the paucity of foreign investment, loans from multilateral institutions, in particular, the IMF and the World Bank, and bilateral development assistance agencies like USAID became vital for the economy as sources of financing essential imports and funding development projects.

BURDEN OF DEBT

Several Caribbean countries have become heavily indebted during the last decade. They account for most of the region's US\$14.5 billion external debt. The largest debtors are Jamaica with US\$4.3 billion, the Dominican Republic with US\$3.9 billion, Trinidad and Tobago with US\$2.0 billion and Guyana with US\$1.6 billion. For many countries their debt is large in relation to their total output and productive capacity. In Guyana the debt/GNP ratio is 522% which means that the debt outstanding is 5-1/4 times larger than the economy's total output of goods and services. Put another way, it would take five and a quarter years to pay off the amount if the output of all economic activity was devoted exclusively to this purpose.

The servicing of the external debt has become the single most sustained impediment to economic growth. The debt service ratio, i.e. the share of foreign exchange earnings from exports of goods and services required for debt repayment is high (e.g. in 1988 it was 16.3% in Belize, 16.1% in the Dominican Republic and 17.4% in Haiti). In Jamaica it was 39.3% which means just under half of every US dollar earned is not available to the economy to purchase essential imports such as oil, food, spare parts, capital goods and medicine.

These high debt servicing ratios are made more onerous by the fact that the highly indebted countries are simultaneously encountering a net transfer of resources.

In Jamaica in 1988, the net transfer was negative, i.e. repayment exceeded new loan inflows and amounted to US \$406 million or 23% of exports of goods and services. The net negative transfer was US\$56 million in the Bahamas, US\$20 million in Haiti, US\$199 in the Dominican Republic and US\$13 million in Belize. This is extremely debilitating to these developing countries which on the contrary should aim to receive a new inflow of resources to reinforce the process of economic growth and facilitate structural transformation.

In many countries debt repayment is the major factor preventing

(1) reduction of fiscal deficits and

(2) the increased capacity of the government to provide infrastructure, health, education, and security. Debt repayment consumed 40% of government expenditure and 54% of revenue in Jamaica in 1988-89. It required 26.3% of government revenue in Antigua, 24% in Grenada, and 34% in St. Kitts

In Jamaica every US dollar earned is not available to the economy to purchase essential imports such as oil, food, spare parts, capital goods and medicine.

WORSENING DEBT CRISIS

The debt of the Caribbean region has more than doubled, from approximately US\$6.1 billion in 1980 to US\$14.3 billion in 1988. During the 1980s debt has more than doubled in Haiti, Jamaica, Guyana and Trinidad and Tobago. In Barbados the debt has increased by 450% and in Antigua by 515%. The debt/GNP ratio for Guyana jumped from 139% in 1980 to 521.8% in 1988, while in Jamaica it moved from 76.5% to 154.1% and in Antigua it leaped from 69.4% to 354.6%.

The worsening situation is also evident in the increase in debt repayment by 50% during the years 1980 to 1988, from US\$1.07 billion to US\$1.56 billion. The most dramatic increases have been in Barbados, Jamaica, Haiti and the Bahamas with increases of 352%, 215%, 258%, and 217% respectively. Negative net transfer of resources has increased in the last few years. During 1985 to 1988, Jamaica transferred overseas more than it received in each year totalling US\$1.2 billion for the four-year period. Countries which traditionally were net recipients

have witnessed a change to negative net transfers, namely the Dominican Republic, Guyana, and Trinidad and Tobago.

CARIBBEAN DEBT IS A SPECIAL CASE

The crisis of Caribbean debt is unique and is therefore a special genre of the debt problem. This is because the bulk of outstanding debt is owed largely to official creditors.

This type of debt situation has not received sufficient attention. Debt relief has focused primarily on the commercial bank debt of developing countries and socialist countries of Eastern Europe and on the bilateral debt of low-income countries, particularly those in Africa. The issue of debt owed to multilateral institutions such as the International Monetary Fund, the World Bank and the Inter-American Development Bank has not been tackled because these institutions do not reschedule debt. Bilateral or inter-governmental debt has been the subject of numerous and repeated rounds of rescheduling through the Paris Club mechanism.

Debt to official creditors (i.e. multilateral institutions and bilateral agencies) is extremely high for nearly all Caribbean countries. The share of official debt in public and publicly guaranteed long-term debt is 91.1% in Haiti, 85.9% in Jamaica, 78.8% in Guyana and 75.4% in the Dominican Republic.

Debt due to multilateral institutions is 65.2% in Haiti, 45.3% in Guyana, 39.9% in Jamaica, and 25-30% in Barbados, the Dominican Republic and the OECS countries of the Eastern Caribbean. Bilateral debt is a particularly large share in the Dominican Republic and Jamaica where it accounts for 47.4% and 46.4% respectively.

The predominant share of official debt in the long-term debt of Caribbean countries indicates that the debt was accumulated in the quest for economic development through projects and infrastructure and/or stabilization cum adjustment.

One of the dilemmas of the debt crisis is that there seems to be no reward for good behavior. In other words,

countries which make strenuous efforts to achieve stabilization and adjustment and pursue sound economic management, and which are reliable in their debt repayment, do not receive more favorable treatment in terms of debt rescheduling from commercial banks, governments of creditor countries and multilateral institutions, in particular, the IMF. The inconsistencies in the secondary market also seem to reward those debtors which do not honor their obligations, instead of rewarding countries which abide by their repayment schedules and conduct their fiduciary affairs responsibly. This is illustrated by the fact that countries which are reliable in their debt servicing find that their debt is sold in the secondary market at a higher price than the debt of countries which are in arrears.

DEBT RELIEF IMPERATIVES

Reduction of the stock of outstanding debt and the complimentary reduction of repayment on a meaningful scale must commence immediately. All three types of debt must be addressed, namely, commercial bank debt, multilateral debt and bilateral debt.

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I. COMMERCIAL BANK DEBT

Commercial bank debt will have to be subjected to rescheduling on much more generous terms, i.e., terms which realistically reflect the debtor countries' repayment capacity rather than the portfolio management and loan-loss considerations of the banks.

II. MULTILATERAL DEBT

The multilateral institutions cannot simultaneously urge reduction measures on other creditors while eschewing any form of rescheduling. The argument that the viability and credit rating of these institutions would be jeopardized is not credible since their soundness derives not from their operations but from the backing of the developed countries. If supplementary resources or charter changes are required to enable these institutions to undertake debt restructuring then this must be done and quickly.

III. BILATERAL DEBT

Consider the following:

(a) The rescheduling of bilateral or inter-government debt must be on more realistic terms, involving longer repayment and grace periods, and lower interest rates of both interest and principal. The futility of rescheduling on terms granted to date is demonstrated by the perpetual cycle of debt restructuring. Since 1980, the United States government has negotiated and signed over 140 Paris Club debt rescheduling agreements totalling US\$15 billion owed by 60 countries. Many countries have had more than one rescheduling, seven countries have had four or more and one country has had nine. In the eleven years between 1968 and 1979 there were 12 agreements but in the ten years 1980 to 1989 there have been 116 reschedulings. There were 23 in 1989 and 9 in the first four months of 1990. The amount of debt involved has increased significantly, from US\$2.2 billion during 1980-1985 to US\$11.7 billion since 1985.

(b) There comes a point where creditors recognize that debt owed to them is unpayable and uncollectable. The debt of many developing countries, including some Caribbean countries, can only be paid at the detriment of both the debtor and creditor country. The cancellation of inter-government debt has been advocated in the case of the poorest countries, but has been implemented on a small scale by a few creditor countries including France, the Netherlands, Sweden, Switzerland, West Germany, Canada and the Soviet Union. The cancellation of debt is not new nor unprecedented as there are several examples involving the debt of both developing and developed countries. At the end of World War I the Allies owed the United States over US\$12 billion. After several interruptions in repayment and the accumulation of substantial arrears, these debts were rescheduled, the repayment periods extended, principal sums reduced or cancelled and the interest rate reduced. Only US\$2.6 billion was repaid between 1918 and 1931, less than quarter of the original sum. In 1940 the British Treasury wrote off 11.2 billion pounds Sterling owed by the colonies.

(c) Significant debt relief could be afforded Caribbean economies if inter-government debt could be repaid in local currency and these funds recycled as grants to be applied to approved development projects or programs. This would provide relief in two important respects: (1) it would save on foreign exchange for debt repayment, increasing uniform capacity and thereby increasing economic growth; and (2) it would replenish fiscal resources with what would otherwise be lost to government.

DEBT RELIEF NOW

In conclusion, the United States cannot be an oasis of well being in a sea of poverty. The debt crisis of Caribbean countries, which has not been adequately addressed in terms of tangible debt relief, has adverse implications for the economy and society of both the United States and the Caribbean. Given the small size of the debt and given that debt reduction for reconstruction and development is not

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unprecedented, the U.S. could take steps to afford debt relief. One practical measure is to allow debt owed to the U.S. to be repaid in local currency and to recycle these funds as grants to be applied to approved development projects. Such debt relief would have a significant impact because it would save foreign exchange which could then be used for development projects leading to economic growth. Debt relief provided now would impact on the Caribbean at a critical juncture and could obviate the need for much larger development assistance and debt relief at a later date.

The U.S. has taken an initial small step through its Enterprise for the Americas Initiative (EAI) towards providing relief to heavily indebted countries in Latin America and the Caribbean. However, the EAI provides long-term relief through a write-down in the stock of debts owed to the U.S. Because of the decision that debt relief should be "budget neutral" for the U.S. Federal budget, payments would remain at the existing level, thereby affording no cash flow relief in the short term. ♦