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THE VICIOUS CIRCLE OF FOREIGN INDEBTEDNESS:
THE CASE OF JAMAICA

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ECONOMIC DEVELOPMENT

Economic development is a process which involves both a qualitative and a quantitative dimension, i.e., economic growth and structural transformation. The rate of economic growth is determined by capital accumulation which is a function of investment. Investment depends on the level of domestic savings and the volume of capital inflows. An unshakable tenet of development economics since the 1950s has been that the main constraint to a take-off in self-sustaining economic growth in underdeveloped economies is the shortage of capital. The central problem of development economics Arthur Lewis has stated is "to understand the process by which a community which was previously saving and investing four or five percent of its national income or less, converts itself into an economy where voluntary savings is running at about twelve to fifteen percent of national income or more."¹

The diagnosis of underdevelopment is frequently that development and economic growth are synonymous and the rate of economic growth is inadequate because of inadequate investment. There is inadequate investment because underdeveloped economies are locked into a vicious circle of poverty,² or in Nurkse's succinct phrase, "A country is poor because it is poor."³ Low incomes cause low savings (supply) and low demand (demand), both of which cause low investment, which in turn causes low productivity and therefore low income. This binding circle idea has become ubiquitous in the litera-

¹W. A. Lewis, Economic development with unlimited supplies of labour, The Manchester School (May, 1954). Reprinted in A.N. Agarwala and S. P. Singh, Oxford University Press, New York, 1958, p. 415 and Some Aspects of Economic Development, University of Ghana, 1959, pp. 75-77.

²R. Nurkse, Problems of Capital Formation in Underdeveloped Countries and Patterns of Trade and Development, Oxford University Press, New York, 1957, pp.4-5.

³Op. cit., p.4.

ture being attributed not only to poverty but to overpopulation,⁴ e.g., Nelson's Low Level Equilibrium Trap,⁵ and to traditional values and social structures which retard enterprise.⁶ This so-called capital "deficiency" is aggravated by "prodigal consumption or short-term speculative investment" rather than productive investment.⁷ The vicious circle of inadequate capital accumulation could only be broken by an inflow of foreign capital whether as a shock, e.g., a "big push",⁸ or sustained over a period of years accepted widely and constitute the justification for development aid and multilateral aid institutions. The assumption of capital deficiency and remained implicit, but nonetheless informed development policy of governments in both the developed and developing countries and international institutions. For example, the Jamaican Government's Five Year Independence Plan, 1963-1968, states that: "The shortage of capital is probably the most serious problem facing most underdeveloped or developing countries. One of the main factors is the deficiency of market demand which tends to keep down private investment because of low real purchasing power. The low level of purchasing power is related to the low levels of income which in turn is basically a result of low productivity. These contributory causes result in a circle which is difficult to break."¹⁰

The idea that a period of foreign capital inflows is inevitable and indispensable was formulated into a pseudo-historical theory of stages of development. All countries, it is claimed, start as "young debtors" when imports exceed exports and domestic investment exceeds domestic savings because of inflows of foreign capital. Growth occurs and the country evolves through "mature debtor" and "new creditor" to the "mature creditor"

⁴Articles and books are too numerous to mention. Its widespread acceptance is indicated by the fact that it is presented in text books of economic development, e.g., J. Viner, International Trade and Economic Development, Oxford University Press, New York, 1953, pp. 105, 133. G. M. Meier and R. E. Baldwin, Economic Development, Theory, History and Policy, John Wiley, New York, 1957, p. 319; W. Krause, Economic Development, Wadsworth, New York, 1951; and H. Myint, The Economics of Developing Countries, Hutchinson University Press, 1954.

⁵R. R. Nelson, A theory of the low level equilibrium trap, American Economic Review, 65 5 December (1956), pp. 894-905.

⁶W. W. Rostow, The Stages of Economic Growth, 2nd. ed. Cambridge University Press, New York, 1971, pp.6-7, and H. Leibenstein, Economic Backwardness and Economic Growth, John Wiley, New York, 1957.

⁷G. M. Meier and R. E. Baldwin, Economic Development, Theory, History and Policy, John Wiley, New York, 1966, pp. 306-307.

⁸P. N. Rosenstein-Rodan, Problem of industrialization of eastern and south-eastern Europe, Economic Journal, June-September (1943), pp. 202-211, and Notes on the theory of big push. In H.S. Ellis and H. Wallich (Eds.), Economic Development for Latin America, Macmillan, New York, 1961, pp. 57-66.

⁹A. O. Hirschman, The Strategy of Economic Development, Yale University Press, New Haven, 1958.

¹⁰The Five Year Independence Plan 1963-1968, Government Printer, Kingston, 1965, p. 28.

stage, exporting capital as exports exceed imports and domestic savings exceed domestic investment.¹¹ It was argued that the presently developed countries had become capital exporters having benefitted from foreign investment in the early stages.¹² The extension of this line of thought led to the programming of the amount of capital required over a specified period to transform an underdeveloped country through the stages to a state of self-sustaining economic growth. Since the volume of foreign investment was uncertain and usually inadequate especially for the poorest countries, the question became what was the amount of aid required to achieve the warranted rate/over what time period.¹³ The assumption was that capital inflows would eventually create an internally dynamic self-sustaining process of capital accumulation.

This blind faith in the procreative power of foreign capital has been questioned by several empirical studies. Griffin and Enos show that for fifteen African and Asian countries during 1952-1964 there was no close association between the amount of external assistance (aid) and the rate of growth of GNP. They also found a negative relationship for twelve Latin American countries for the present period 1957-1954.¹⁴ Weisskopf¹⁵, and Rahman¹⁶ state that foreign aid adversely affects domestic savings. The reason being that domestic savings are substantially determined by government policy and the government's savings effort and that the latter will be less vigorous if external assistance is available. Singh has concluded that there is a high "substitution of capital inflows for national

¹¹P.A. Samuelson, Economics, 7th ed. McGraw-Hill, New York, pp. 635-637. C.P. Kindleberger, International Economics, 4th ed., Irwin, Homewood, 1968, pp. 483-485 and B. A. deVries, The debt bearing capacity of developing countries - a comparative analysis, Banca Nazionale del Lavoro, Quarterly Review 96, March (1971), pp. 65-68.

¹²For critiques of this theory, see K.E. Berrill, Foreign capital and take-off. In W. W. Rostow (Ed.), The Economics of Take-off in Sustained Growth, Macmillan, New York, 1963. Also, A. K. Cairncross, Factors in Economic Development, Allen and Unwin, Boston and London, 1962. Chap. 3.

¹³H. Chenery, Foreign assistance and economic development. In J. H. Adler (Ed.), Capital Movements and Economic Growth, Macmillan, London, 1967, pp. 268-287. H. Chenery and A. Strout, Foreign assistance and economic development, American Economic Review, 56 4 Part I, September (1966), pp. 679-733. H. Chenery and I. Adelman, Foreign aid and economic development: the case of Greece, Review of Economics and Statistics, February (1966). Also, H. Chenery and A. MacEwan, Optimal patterns of growth and aid: the case of Pakistan. In I. Adelman and E. Thorbeckes (Eds.), The Theory and Design of Economic Development, John Hopkins Press, Baltimore, 1966.

¹⁴K. R. Griffin and J. L. Enos, Foreign assistance: objectives and consequences, Economic Development and Cultural Change, 18 April (1970), pp.317-325.

¹⁵T. Weisskopf, The impact of foreign capital inflow on domestic savings in underdeveloped countries, Journal of International Economics, 2 1 February (1972) pp.25-38.

¹⁶A. Rahman, Foreign capital and domestic savings: a test of Haavelmo's hypothesis with cross-country data. Review of Economics and Statistics, 50, 1 February (1968).

savings."¹⁷ Areskoug using time series of 10 to 12 annual observations of 22 developing countries concludes that "it is highly questionable whether the steady flow of long-term, but repayable, capital to underdeveloped countries in the end contributes to their domestic capital formation and growth potential."¹⁸ For many of them, the domestic capital stock may ultimately be reduced through their external borrowing, in spite of low interest charges." Areskoug's conclusion rests on the reasoning that since part of the foreign borrowing finances domestic consumption as well as investment, new savings made possible from future income streams will be unable to counter-balance foreign amortization payments. Papanek's cross-country study finds that aid and growth are positively related but aid and domestic savings are negatively related.¹⁹ Mosley, has shown that financial foreign aid is negatively related to economic growth.²⁰ Griffin found that the outflows of profits and interest payments exceeded new capital inflow net of amortization in Latin America over the period 1951-1966.²¹

VICIOUS CIRCLE OF FOREIGN INDEBTEDNESS

In developing countries a vicious circle of foreign indebtedness develops where the country has to borrow, but it is only raising sufficient foreign capital by attracting foreign investment and loans, to enable it to meet current payments of interest, principal and profits due from the already existing stock of foreign capital and foreign debt. Developing economies are vulnerable to being locked into a vicious circle of foreign indebtedness. The process of capital accumulation in developing economies is externally dependent i.e., there is only a limited internal dynamic of accumulation. Dependent accumulation is determined by the amount of foreign capital available to the economy. Production has a high import content, therefore capital accumulation depends on import volume which is determined by the quantum of foreign exchange. The amount of foreign exchange is determined by export earnings and capital inflows. Inflows of foreign capital increase the level of investment and provide foreign exchange. However, payments on capital flow out of the economy reducing funds available for investment and foreign exchange for imports. Dependent accumulation is not a stage on the way to development nor is foreign capital the catalyst. Foreign capital retards accumulation as it reinforces dependence as manifested in the vicious circle of foreign indebtedness. The vicious circle of foreign indebtedness is inherent in dependent accumulation and has a tendency to decapitalize the economy, i.e., underdevelopment with stagnation. Only in favourable periods does the vicious circle permit growth,

¹⁷S.K. Singh, The determinants of aggregate savings, World Bank, Economic Staff Working Paper, 127 (1968)

¹⁸K. Areskoug, External Public Borrowing: Its Role in Economic Development Praeger, New York, 1969.

¹⁹G. F. Papanek, Aid, foreign private investment and growth in less developed countries, Journal of Political Economy, 81 1 January/February (1973).

²⁰P. Mosley, Aid, savings and growth revised, Oxford Bulletin of Economics and Statistics, 42 2 May (1980).

²¹K. Griffin, Foreign capital, domestic savings and economic development, Bulletin of the Oxford University Institute of Economics and Statistics, 32 May (1970) pp. 99-112.

i.e., underdevelopment with growth.

FOREIGN CAPITAL IN THE JAMAICAN ECONOMY

Jamaica has a long tradition of dependence on inflows of foreign capital, a dependence rooted as much in the structure of the economy as in the belief that the country is too small to achieve self-sustaining growth.²² Foreign capital has been critical to the economy in two ways. First, the persistent current account deficit in the balance of payments was in some years financed by a new inflow of capital.²³ This facilitated imports in excess of export earnings in those years. Secondly, during the years 1951 to 1980, foreign capital inflows financed 29.2 percent of gross investment and in 1981 it accounted for 57 percent. See Table 1.

Foreign capital can contribute to economic growth in developing countries like Jamaica, but in some cases it can denationalize ownership and decision-making, resulting in sizeable outflows of profits and payments.²⁴ Both political parties see a role for foreign capital in the country's economic development, but differ on the form and operating conditions. The Peoples National Party regards foreign capital inflows as important, but places the emphasis on aid (loans on concessionary terms) and commercial loans rather than private direct foreign investment. Foreign investment is seen as having a number of disadvantages and is most fecund when regulated and confined to specific sectors. The Jamaica Labour Party's position is that, not only is foreign capital indispensable to economic growth, but it must take the form of private direct foreign investment, since it is believed to be procreative and catalytic.

Prime Minister Seaga has argued that domestic savings is insufficient and local entrepreneurship is inadequate, so economic growth depends on "what aid can be salvaged and what investments can be managed."²⁵ Therefore, "the first essential is that developing countries should ensure that a favourable climate exists for foreign investment."²⁶

²²This myth had its origins in the colonial period, see L. Lindsay, Colonialism and the myth of resource insufficiency in Jamaica. In V. Lewis, (Ed.), Size, Self-Determination and International Relations: The Caribbean, Institute of Social and Economic Research (ISER), University of the West Indies (UWI), Mona, Jamaica, 1976, 45-72.

²³See R. Bernal, Jamaica's balance of payments (1960-1980), Housing and Finance, Winter (1983) 26-37, 34 and 35.

²⁴R. L. Bernal, Foreign investment and the Jamaican economy, Housing and Finance Winter (1981), 3-5.

²⁵Statement of the Rt. Hon. Edward P. G. Seaga, Prime Minister of Jamaica, concerning the Caribbean and Central America Revitalization Act. Presented to the Senate Committee on Finance, United States Senate, Washington D.C., August 11, 1982, 4-5.

²⁶For an analysis of policy differences on foreign investment and foreign loans see R. L. Bernal, Economic growth and external debt in Jamaica. In A. Jorge, J. Salazar-Carrillo and R. P. Higonnet (Eds.), External Debt and Economic Growth in Latin America, Pergamon Press, London and New York, 1982.

One specious argument put forward in favour of direct foreign investment in preference to foreign loans, is that loans have to be repaid with interest but foreign investment does not necessarily involve this kind of outflow. This is a fallacy as the Jamaican experience during 1960 to 1980, clearly demonstrates. A comparison of the outflow of investment income (profits on investment and interest on debt) with net capital movements (private and officials) shows that investment income exceeded net inflow of capital in every year, between 1960 and 1967 and again between 1976 and 1980. During the period 1968 to 1975, there was a surplus due to investment in the Bauxite/Alumina industry and the heavy borrowing of 1973-1975. The decapitalization of the country between 1960 and 1980, was US \$461.7 million. See Table 2. Apart from the disparity in flows, another consideration is that foreign investment involves loss of control of the country's resources, while loans for capital investment, permits the retention of national ownership and decision-making. However, foreign borrowing by the government can simultaneously increase investment and reduce relaxation of efforts to maintain or increase domestic savings. The government's external debt operations, raises the level of capital formation by increasing public sector investment and private investment through loans from public sector financial institutions, but reduces domestic savings as the fungibility of loans permits substitution of foreign funds for local funds in investment projects. Also, the escalation in the debt servicing eventually reduced revenues available for current and capital expenditures.²⁷

FOREIGN DEBT

Foreign borrowing is a tenet of fiscal policy in Jamaica, especially since independence. The practice of financing part of the capital expenditure with foreign loans was well established by the 1950s.²⁸ Until the mid-1970's most of the foreign borrowing was in the form of commercial loans, by the issue of stocks on the London capital market and after 1959, on the New York market, with the first Canadian issue in the fiscal year 1964-1965. In 1967, there were two new developments, the first loan from a commercial bank was negotiated with the Bank of Nova Scotia and the first World Bank loan commenced disbursement. The pattern of government's foreign borrowing, that is the national external debt, is the dominance of commercial loans from 1946 to the mid-1970s, with concessional loans predominance after 1978, (see Table 3). Loans from transnational commercial banks grew rapidly in 1973, 1974 and 1975, reaching a peak of 60.9 percent of the gross external debt in December 1975 (see Table 4).

Jamaica's gross external debt was very small during the 1950s and 1960s, reaching J\$ 100 million in 1970, with debt payments accounting for 4 to 5 percent of both export earnings and government revenues.²⁹ The external

²⁷See C. Bourne, Government foreign borrowing and economic growth: the case of Jamaica, Social and Economic Studies, 30 4, December (1981), 52-74.

²⁸Budget Speech, Hon. D.B. Sangster, Government Printer, Kingston (1954) 35.

²⁹For information on foreign debt between 1945 and 1970 see N. Girvan, Foreign capital and economic underdevelopment in Jamaica, ISER/UWI, Mona, Jamaica, 1971. Chap. 6. And, C. Kirton, A preliminary analysis of imperialist penetration and control via the foreign debt: a study of Jamaica. In C. Stone and A. Brown (Eds.) Essays on Power and Change in Jamaica, Jamaica Publishing House, Kingston, 1977, pp. 72-88.

debt doubled between December 1973 and December 1975, when it amounted to U.S. \$420 million. This was largely accounted for by increases in loans from transnational banks of 132.1 percent in 1973, 146.4 percent in 1974, and 54.2 percent in 1975 (see Table 4). The gross external debt doubled again between December 1974 and December 1980, when it stood at US \$ 895.9 million (see Tables 5 and 6). In the two and a half years up to June 1983, the debt has increased by 42.6 percent, with each new loan being hailed as a sign of confidence in the management of the economy.³⁰ Indeed, in its first two years in office (1981 and 1982) Mr. Seaga borrowed over US \$1 billion, including US \$427.2 million from the IMF, with most of the rest being special loans from the United States Government.³¹

CAUSES OF BORROWING

The policies of both the Manley and Seaga Governments have aggravated the vicious circle of foreign indebtedness. The Manley Government responded to the major economic crisis of the mid-1970s, by trying to maintain economic growth by foreign borrowing while undertaking a structural transformation towards a more self-reliant mixed economy. Three exogenous developments adversely affected the Jamaican economy in the mid-seventies.³² a) There was a marked slow-down in world trade, as trade grew at 5.7 percent per annum in the 1970s, compared to nearly 8 percent per annum in the 1960s.³³ b) Inflation in the world accelerated, spurred by a four-fold increase in oil prices in 1973-1974. c) There was a sharp decline in direct foreign investment during the period 1972-1974. This deterioration in the world economy was compounded by unfavourable domestic developments between 1974 and 1975. These included: d) declines in export volume in 1975-1976. e) A fall in export prices 1975. f) A decline in receipts from tourism in 1976. g) Significant increases in the outflow of private capital and investment income. The balance of payments which in 1970 had registered a surplus of 6.9 million was by 1972, showing a deficit of -J\$ 40.6 million, which increased further to -J\$ 231.3 million in 1976.

The Manley administration decided to pursue a policy of fiscal expansion. The objective was to stimulate growth and finance the balance of payments deficit on the assumption that the recession in the world economy was temporary. Fiscal expansion was to be financed by foreign borrowing and increased government expenditure would increase aggregate demand and induce

³⁰In November 1982, Mr. Seaga spoke of a US \$79 million loan from commercial banks as "the most important indicator that we were on our way to restoring the confidence of the international financial community in Jamaica." See The Second Year, Jamaica Information Service, Kingston, 1982, p. 5.

³¹Bank of Jamaica, Annual Report 1982, p.5.

³²This section draws on R. Bernal, Jamaica's balance of payments (1960-1980), Housing and Finance, Winter 1982. And also on N. Girvan, R. Bernal and W. Hughes, The IMF and the Third World: the case of Jamaica, 1974-1980, Development Dialogue, 2, (1980) 134-140.

³³World Bank, World Development Report 1981, Washington, D.C., p. 8.

increased output and employment.³⁴ A higher level of demand would not generate imports, because of the imposition of import restrictions, which would furnish opportunities for import substitution. Control of inflation was to be achieved by restrictive credit policies. It was decided that the budget deficit should be financed by foreign borrowing rather than by increased taxation or local borrowing. Increased taxation would be required but this was ruled out, because it was felt that it would increase the cost of living, reduce demand and might discourage investment. Tax revenue from the bauxite/alumina industry which would have none of these repercussions, was increased from J\$41 million in 1973, to J\$174.9 million in 1974, by the imposition of the Bauxite Production Levy. Increased local borrowing was used as little as possible in the early years, because it would reduce loanable funds available to finance investment and production in the private sector. The government was not able to adhere to this position and increased its local borrowing as the deficit grew. Foreign borrowing was seen as the best option because a) the public sector would make minimal demands on domestic loanable funds, leaving it for the private sector, b) Foreign borrowing would cover the import content of the budget (19-23 percent) making no demand on the limited foreign exchange available and, c) foreign loans equal to the budget's import content, would not generate inflation as there would be no expansion of money supply.

There were problems with this policy, the principal ones were:

1. The recession in the world economy did not abate but continued.
2. As the economy contracted, the demands on the budget multiplied and intensified, for example, expenditure on social programmes to alleviate unemployment, illiteracy, malnutrition and poverty. Mr. Manley felt that these programmes were socially desirable and were "the price of survival of the democratic system."³⁵
3. Inflation which was 26.9 percent in 1973 and 20.6 percent in 1974, added considerably to the cost of operating the state apparatus. Inflation meant that in order to maintain expenditure in real terms, expenditure in money terms would have to be increased by the equivalent of the rate of inflation generated demands for compensatory wage increases. The wage bill of the government tripled between 1971 and 1975, from J\$ 107.9 million to J\$ 328 million. This, of course, reflected not only inflation inspired wage increases, but also deliberate expansion of employment programmes.
4. The inadequate and inefficient system of financial accounting in the state bureaucracy, led to overexpenditure.³⁶ A crude indicator of resulting overexpenditure is the magnitude of the difference between original approved estimates of recurrent expenditure and final outturn. The outturn

³⁴The following section draws heavily on R. L. Bernal, Transnational commercial banks, the International Monetary Fund and capitalistic crisis in Jamaica 1972-1980. In J. Estevez and S. Lichtenestejn (Eds.), *Nueva Fase del Capital Financiero. Elementos Teóricos y Experiencias en América Latina*, ILET/CEESTEM, Editorial Nueva Imagen, Mexico City, 1981, pp.281-334.

³⁵Budget Debate Speech, Hon. M. Manley, Prime Minister of Jamaica, May 1, 1972, Government Printer, Kingston, 1972, p. 6.

³⁶Public financing under review, *Jamaica Daily News*, 7 December 1974, pp.18-19.

exceeded estimates by 10 percent in 1973-1974 and by 20 percent in 1974-1975.³⁷

The transnational commercial banks suspended lending to Jamaica in 1976, pending the implementation of an IMF designed programme of balance of payments adjustment. New loans from the banks were a benefit Jamaica hoped to gain from having an IMF programme, but this did not materialize as the banks concentrated on ensuring repayment, during 1976-1980.³⁸ An IMF programme is a necessary but not sufficient condition for borrowing from the transnational commercial banks.³⁹ Mr. Manley eloquently described the dilemma when he said: "When the IMF lends money, it is not allowed to lend you enough. The banking system is supposed to lend you the rest. But the banking system is not an umbrella for aid. It is a parasol for bright weather."⁴⁰

JAMAICA'S VICIOUS CIRCLE

Blondie: Here is the ten dollars I owe you.

Dagwood: Thanks!

Blondie: Can you lend me ten dollars?

Dagwood: O.K. but why bother to pay back the first ten dollars?

Blondie: So I could borrow it again!⁴¹

Jamaica is now locked into a vicious circle of foreign indebtedness where it is borrowing just enough to meet its debt repayments. In the six years between 1977 and 1982, loan receipts totalled US \$ 2.1 billion while repayments on public and private debt amounted to US \$ 2 billion (see Table 7).

During 1981 and 1982, over 50 percent of the cash inflow from gross exports of goods and services was used to repay foreign debts (see Table 8). The debt service, that is the ratio of debt payments to gross exports of goods and services, has increased from 5.4 percent in 1974, to 29.5 percent in 1982 (see Table 9), indicating a significant increase in the burden of foreign indebtedness. The country's total foreign debt, includes direct government debt usually called the National "external debt," government guaranteed external (foreign) debt, the foreign liabilities of Bank of

³⁷Calculations based on Memorandum on the Budget 1973-75, Ministry of Finance, May 6, 1974, and Memorandum on the Budget 1975-76, Ministry of Finance, May 15, 1975.

³⁸Bank of Jamaica, Annual Report 1978, p. 1

³⁹R. L. Bernal, Transnational banks, the IMF and external debt of developing countries, Social and Economic Studies, 31 4 December (1982) 71-101.

⁴⁰Address by Hon. M. Manley, Prime Minister of Jamaica to the 20th Annual Meeting of the Board of Governors, Inter-American Development Bank, Montego Bay, Jamaica, 28th May, 1979.

⁴¹I am grateful to Cheryl Payer for bringing this issue of the cartoon to my attention.

Jamaica, which include debts owed to the IMF and private debt. No published figures on private debt are available, but the total of the other categories reveals a debt of J\$ 5.2 billion or US \$ 2.9 billion in June, 1983. This is roughly the equivalent of the country's Gross Domestic Product in 1981, that is, the total of all goods and services produced in Jamaica in that year. As is, it is an underestimate as it does not include private debts and lines of credit.

TIGHTENING THE VICIOUS CIRCLE

The Seaga government has sought to stimulate economic growth by heavy foreign borrowing. The government borrowed over US \$1 billion dollars in its first two years on the basis that economic growth depends heavily on the amount of foreign exchange available for imports. The Prime Minister has stressed that foreign borrowing has been made necessary by high debt repayments, due to the borrowing of the previous government and the deferral of debt payments payable in 1978-1979.⁴² A strange complaint, given that Mr. Seaga resorted to refinancing US \$103 million in 1981.⁴³ The Government also raised US \$71 million for seven years at 2 1/4 percent Libor from a syndicate of twenty-seven commercial banks led by Citibank.⁴⁴ The Seaga administration has not been able to secure new loans from the transnational banks although it tried in late 1982.⁴⁵ Banks are not impressed by claims of how much better the government is performing than its predecessor,⁴⁶ nor in prognostications of unprecedented levels of investment on the basis of investment proposals.⁴⁷ Banks scrutinize realistic appraisals of the actual performance of the economy and assess its future prospects. The present government cannot claim successful management of the economy, since it has twice failed to pass the IMF stipulated targets in 1983. Not surprisingly, Jamaica's credit rating has not improved (see Table 10) and a Seaga administration rescheduling proposal was turned down by the banks in 1983.

Attempts by both Manley and Seaga governments to reschedule the most costly part of the external debt, that owed to transnational commercial banks, have failed.⁴⁸ However, a number of refinancing operations have been undertaken. In 1975, US \$5.5 million of original loans totalling US \$11 million, was refinanced by Manufacturers of Hanover, Citibank and Citizens

⁴² Budget Speech 1983, see Balance sheet by the Prime Minister, Daily Gleaner 8 May 1983, p. 16.

⁴³ R. Forrest, International credit flows, Sunday Gleaner, 19 July 1981.

⁴⁴ \$70 million loan to Jamaica oversubscribed, Daily Gleaner 8 July 1981.

⁴⁵ P. Kenyon, Seaga plans to raise US \$30 million in two months from European banks, Daily Gleaner 4 September 1982.

⁴⁶ Statement to Parliament by the Rt. Hon. E. Seaga, November 3, 1981, JIS (1981), and statement by the Prime Minister, Rt. Hon. E. Seaga to the House of Representatives, November 2, 1982, JIS (1982).

⁴⁷ Seaga: 4 percent growth this year, Daily Gleaner, 8 March 1982, p. 1.

⁴⁸ Thumbs down on Jamaica, Jamaica Daily News 16 September 1979, p. 1.

and Southern Bank.⁴⁹ In June 1979, a Deferral and Refinancing Agreement was concluded with a syndicate of 85 transnational commercial banks led by Citibank and the Royal Bank of Canada. The agreement provided for the deferral of US \$126 million of principal payments on direct government debt and debt of government owned corporations.⁵⁰ In March 1981, eight banks agreed to defer and refinance US \$103 million of principal falling due between April 1981 and April 1983. This was converted into a six-year loan at 1.75 percent above LIBOR with a three year grace period.⁵¹ At present the Seaga government is making another rescheduling proposal to the transnational commercial banks.

DEBT POLICY

An appropriate and viable debt policy for Jamaica must be based on recognition that:

1. Genuine economic development is not possible with the economy locked in a vicious circle of foreign indebtedness.
2. The country cannot borrow its way out of the vicious circle of foreign indebtedness.
3. The real problem is that since 1960, the economy has failed to earn enough foreign exchange to meet its demands.
4. The solution involves structural transformation of the economy to align foreign exchange earnings with demand at a level which generates economic growth.
5. Structural transformation is a medium term policy. In the short term an appropriate debt policy is germane.

An appropriate and viable debt policy must entail the following:

1. An strict limit on further foreign borrowing. This will undoubtedly be one of the requirements in any future IMF programme. Whatever the actual figure decided on, there are three criteria which should guide future borrowing:⁵²
 - a) the efficiency criterion; b) the transformation criterion; and c) the liquidity criterion.

⁴⁹ Financial Statements and Revenue Estimates for 1976-1977, Ministry of Finance, May 13, 1976, p. 21.

⁵⁰ 220 million debt case, Jamaica Daily News, 14 June 1979, and Bank of Jamaica.

⁵¹ R. Forrest, International credit flows, Sunday Gleaner, 19 July 1981, and C. S. Hardy, Rescheduling developing country debts, 1976-1981. Lessons and recommendations, Overseas Development Council, Monograph 15, Washington, D.C. June (1982) 38.

⁵² R. L. Bernal, Jamaica's external debt and its implications, National Planning Agency, Kingston, August (1977), Mimeo, pp. 12-13.

The efficiency criterion requires that the yield of the loan, that is, the increase in output resulting from it, must exceed the cost of repayment. Obviously, this implies that loans must be used for productive investment and not for consumption. The transformation criterion is met if the output resulting from the foreign debt financed investment generates sufficient foreign exchange earnings or savings to amortise the loan. The liquidity criterion addresses the problems of timing and cash flow. Even if the transformation criterion is met, the foreign exchange earnings might not coincide with the repayment schedule. This is highly probable where an investment project with a long gestation period is financed by short maturity loans.

2. The debt servicing schedule should be strictly adhered to, avoiding arrears and default.

3. The burden of repayment should, if possible, be reduced by lengthening the repayment schedule by rescheduling and refinancing. Lending institutions rarely agree to rescheduling if the country has not defaulted.

TABLE 1 Average Ratio of Foreign Capital Inflows to Gross Domestic Investment

Time Period	Ratio
1951-1960	32.2
1961-1970	19.6
1971-1980	36.9
1981-	57.0
1951-1970	25.4
1951-1980	29.2
1951-1981	30.1

Source: R. L. Bernal, Foreign investment and the development of underdevelopment in Jamaica, Paper presented at The Caribbean Studies Association Conference, Basseterre, St. Kitts, May, 1984.

TABLE 2 Capital Flows 1960-1982 (J\$ Million)

Year	Capital Outflows				Investment Income	Difference	
	Net Capital Movements	Official	Private	Unidentified		Annual	Cummulative
1960	17.0	6.0	15.5	-4.2	-21.8	-4.8	
1961	10.2	-3.2	22.8	-9.4	-25.0	-14.8	-19.6
1962	7.2	1.6	1.0	4.6	-25.2	-18.0	-37.6
1963	11.4	-4.8	19.0	-2.8	-26.4	-15.0	-52.6
1964	14.9	8.2	3.2	3.5	-28.8	-13.9	-66.5
1965	11.8	6.0	10.2	-4.4	-30.6	-18.8	-85.3
1966	46.7	7.4	46.2	-6.9	-64.8	-18.1	-103.4
1967	64.9	5.0	80.2	-20.3	-67.2	-2.3	-105.7
1968	114.4	12.6	107.6	-5.8	-61.0	+53.4	-52.3
1969	98.5	10.3	88.2		-72.5	+26.0	-26.3
1970	134.1	-1.2	135.3		-81.8	+52.3	+26.0
1971	160.2	4.0	156.2		-85.7	+74.5	+100.5
1972	117.0	18.6	98.4		-100.4	+16.6	+117.1
1973	124.7	33.4	91.3		-52.8	+71.9	+189.0
1974	221.0	81.9	139.2		-61.5	+159.6	+348.6
1975	189.0	112.0	77.0		-93.5	+95.5	+444.1
1976	41.5	72.0	20.1		-105.1	-63.6	+300.5
1977	51.7	-5.4	57.1		-125.6	-73.9	+306.6
1978	8.9	162.6	153.7		-168.8	-159.9	+146.7
1979	-10.5	126.7	-145.2		-360.6	-379.1	-232.4
1980	107.2	369.2	262.0		-416.3	-229.3	-461.7

Source: Bank of Jamaica, Annual Reports.

TABLE 3 Composition of Gross External Debt
March 31, 1946 to December 31, 1982 (%)

Date	Commercial			Concessional
	Market	Banks	Total	
March 31, 1946	80	-	80	20
" 1950	83	-	83	17
" 1954	97	-	87	13
" 1958	89	-	89	11
" 1962	96	-	96	4
" 1966	94	-	94	6
" 1970	66.5	21.5	88	12
December 31, 1974	25.7	55.3	81	19
" 1978	4.7	36.7	41.4	50.9
" 1982	5.1	22.8	27.9	72.1

Source: N. Girvan, Foreign Capital and Economic Underdevelopment in Jamaica, ISER/UWI, (1971) 153, and Bank of Jamaica, Annual Reports.

TABLE 4 Growth of Loans from Transnational
Commercial Banks 1971-1981 (%)

Year	Commercial Bank Loans/ Gross Direct External Debt	Rate of Growth In Outstanding Commercial Bank Loans*
1971	16.7	28.7
1972	17.6	21.3
1973	34.5	132.1
1974	55.3	146.4
1975	60.9	54.2
1976	51.4	-1.8
1977	43.3	-14.9
1978	36.7	16.2
1979	36.3	11.3
1980	31.2	-2.9
1981	29.4	14.6
1982	22.8	2.9
(June) 1983 p	19.4	-8.3

Note: *Based on Debt Figures expressed in US\$.
p Provisional.

TABLE 5 Gross External Public Debt
by Type of Loan - 1971-1981 (\$ Million)

Year	Market Loans	Commercial Banks	International Institutions	Inter- Government	Other *	Total
Dec.1971	64.2	18.4	14.0	13.4	-	110.0
Dec.1972	70.9	22.3	15.1	22.3	0.8	127.6
Dec.1973	66.8	61.2	23.1	23.1	0.9	177.3
Dec.1974	67.7	150.7	25.2	26.3	2.3	272.3
Dec.1975	56.6	232.4	31.2	31.3	30.0	381.5
Dec.1976	41.6	228.2	45.6	99.5	29.0	444.0
Dec.1977	42.2	209.9	65.7	135.1	31.8	484.7
Dec.1978	54.8	435.2	232.2	367.1	95.9	1,185.2
Dec.1979	44.7	499.3	271.2	450.7	110.8	1,176.7
Dec.1980	46.3	497.8	326.9	607.9	115.7	1,594.6
Dec.1981	24.6	570.3	501.0	755.7	89.9	1,942.3
Dec.1982 p	9.0	586.7	778.2	1,043.0	162.8	2,577.7
Jun.1983 p	8.9	537.8	857.6	1,118.3	255.5	2,778.1

Notes: p Provisional
*Includes suppliers credit, public utilities, and other commercial.

Source: Bank of Jamaica

TABLE 6 Breakdown of Gross External Public Debt
by Type of Loan 1971-1981 (US \$ Million)

Year	Market Loans	Commercial Banks	International Institutions	Inter-Government	Other *	Total
Dec .1971	83.4	23.9	18.1	17.5	-	142.9
Dec .1972	92.8	29.0	23.3	20.7	-	165.8
Dec .1973	75.9	67.3	25.4	26.3	-	194.9
Dec .1974	74.6	165.8	27.7	31.5	-	299.6
Dec .1975	62.3	255.7	34.5	36.4	31.1	420.0
Dec .1976	45.9	251.0	50.2	110.4	31.1	488.6
Dec .1977	46.6	213.6	72.2	149.8	51.0	533.2
Dec .1978	32.3	248.3	137.0	216.6	65.0	699.2
Dec .1979	25.1	280.5	152.4	253.2	62.2	773.0
Dec .1980	26.0	279.7	183.7	341.5	65.0	895.9
Dec .1981	13.8	320.4	281.9	424.6	50.5	1,091.2
Dec .1982 p	5.0	329.6	436.0	506.0	91.5	1,448.1
Jun .1983 p	5.0	302.1	481.8	628.3	143.5	1,560.7

Notes: *Includes suppliers credit, public utilities and other commercial.
p Provisional.

Source: Bank of Jamaica.

TABLE 7 Foreign Borrowing and Debt
Repayment 1977-1982 (US \$ Million)

	1977	1978	1979	1980	1981	1982	Total 1977-1982
Loan Receipts	183.5	387.2	292.0	235.0	513.9	512.3	2,123.9
Repayment of Public and Private Debt	217.5	281.8	313.8	282.0	465.4	442.0	2,002.5
Net	-34.0	105.4	-21.8	-47.0	48.5	70.3	121.4

Source: Bank of Jamaica

TABLE 8 Debt Service Ratio 1974-1982 (US \$ Million & %)

	1974	1975	1976	1977	1978	1979	1980	1981	1982
Repayment of Public and Private Debt	53.9	83.2	110.7	132.7	338.8	273.9	263.3	437.8	408.4
Gross exports of goods and Services	999.6	1123.7	945.9	900.6	1919.6	1148.6	1412.3	1506.5	1385.2
Cash Inflow of Gross Exports of Goods and Services	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	800.0	759.3	750.7
Ratio 1:2	5.4	7.4	11.7	14.7	17.6	23.8	18.5	29.1	29.5
Ratio 1:3	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	32.9	57.7	54.4

Source: Bank of Jamaica, Annual Reports, 1975-1982

TABLE 9 Jamaica's Foreign Debt

Type of Debt	Dec. 1977	Dec. 1978	Dec. 1979	Dec. 1980	Dec. 1981	Dec. 1982	June 1983
Direct Government Debt	484.7	1185.2	1376.7	1594.6	1942.3	2577.7	2778.1
Government Guaranteed Debt	318.0	577.5	564.4	573.9	546.0	525.4	506.3
Bank of Jamaica Foreign Liabilities	213.8	530.0	890.2	1022.6	1492.7	1802.7	1963.0
Private Debt	n.a.						

Source: Bank of Jamaica, Annual Reports, various years and Monthly Review,
August (1983).

TABLE 10 Jamaica's Credit Rating by
Institutional Investor 1979-1982

Date	Credit Rating	Rank
September 1979	24.0	82/92
March 1980	19.9	84/96
September 1980	16.5	88/98
March 1981	15.5	90/100
September 1981	16.6	89/104
March 1982	16.8	87/104
September 1982	17.7	83/107
March 1983	n.a.	n.a.

Source: Institution Investor, March (1980) 59; September (1980) 75; September (1981) 207 and September (1982) 284.

DOMINICAN REPUBLIC:
EIGHTEEN YEARS OF ECONOMIC POLICY

Andres S. Dauhajre

INTRODUCTION

The purpose of the present paper is not to analyze the impact on all levels of the economic policies implemented by the democratic governments the Dominican Republic has had since 1966. Such a task would take several years of hard work, as the analysis of the impact of economic policy on all levels would require a careful research of the microeconomic impact of macroeconomic measures.

Our aim is to analyze the impact at a macroeconomic level of the evolution of Dominican economic policy from 1966 on. We will focus on the dynamic evolution of internal and external disequilibria of the Dominican economy and how these have been affected by the economic policies implemented by the different government administrations during the period considered in our study.

First, we will analyze the economic policy of the three administrations headed by the Reformist Party (Partido Reformista), which was initiated in 1966 and finalized in 1978. Then, we will study the new economic policy launched by the Dominican Revolutionary Party (Partido Revolucionario Dominicano), during the period 1978-1982, a party that came into power under the motto of "change." Finally, we will describe the economic policy followed by the second P.R.D. administration, which started in August 1982.

THE ECONOMIC POLICY OF THE REFORMIST ADMINISTRATION: 1966-1978

During the period 1966-1978, the Dominican Republic progressed significantly as to institutional stability and the creation of a favorable climate for national and foreign private investment. The Dominican economy showed an impressive performance during those years. The gross domestic product reached a yearly real growth rate of 11 percent during the period 1968-1974, one of the highest in the world. The real per capita gross domestic product increased \$175.17 pesos, from \$276.82 pesos in 1966 to \$451.99 pesos in 1977. National income more than doubled and a powerful middle class started flourishing in Dominican society. Later on, this middle class would become one of the main bases of support of the Dominican