

# Debt

## - who pays the price?

### The human face of debt

Taking out a loan for a special purpose, or buying things on credit, has become part of modern life. But when people borrow more than they can repay, they may soon become trapped in a cycle from which it is difficult to escape.

On a world scale, the problem of debt refers to money owed by nations. Again, borrowing is an important way for governments to finance national projects such as

telecommunications and energy production. Yet while the decisions about borrowing and lending are made by politicians, bureaucrats and bankers, the effect of indebtedness is felt most by ordinary citizens. When things go wrong, governments find themselves having to meet debt repayments at the expense of services such as public education and clean water.

### The cost of debt ... in Kenya

Jackson is 18 years old. He completed primary school but his parents could not afford the fees for him to continue his education. So he had to look for odd jobs such as clearing bush or tending other people's livestock.

The Kenyan government's structural adjustment reforms (see pages 2-3) included imposing fees for post-primary education, and reducing education spending. Thousands of students could not take up their places. The government pays teachers' salaries, but there is little money for basic tools and equipment, leaving families to bridge the gaps.

### ... in Nicaragua

When Juan Jose was three, he tripped and fell into the fire where coffee was being boiled. He was rushed to hospital and survived, but was left with terrible scars. Since then, he has grown slowly and suffered other health problems. The health centre in his community was closed. His father often cannot find work so the family cannot afford better food or another trip to hospital.

With a country ruined by war and an enormous foreign debt, in the 1990s the Nicaraguan government cut back spending on the health services which had reduced child death rates in the 1980s.<sup>1</sup> Unemployment rose above 60%. By 1995, many Nicaraguans consumed only 1800 calories per day, compared with the recommended 2400 calories. In 1998, the devastating Hurricane Mitch caused further damage to Nicaragua's economy, making its debt more unpayable than ever.

### ... in Tanzania

The parents at Karumi school had a deal with the government. They would pay their children's school fees by building the walls of a classroom for Standard Seven, leaving the government to put on the roof. The parents kept their side of the bargain, but the government did not.

Tanzania is one of the poorest countries in the world. To meet IMF requirements, the government reduced spending on education from 30 per cent in 1960 to 5 per cent of total public expenditure in 1994.<sup>2</sup>

### ... in Mozambique

"Last week I spoke to three mothers whose children had contracted measles, one of whom died. Surprisingly all the children had been immunised, but local staff explained that the vaccines were probably not effective because the government health officers have trouble keeping them cold: sometimes fridges are not available, or not working due to breakdown or lack of fuel."- report from Argentina Matavel, WorldVision Mozambique.

Still recovering from a costly war, Mozambique spends A\$12 per person each year on servicing its debt, compared with A\$4 on health.



In heavily indebted Mozambique, child deaths from measles are still too common.

Reducing the burden of debt cannot guarantee that health care and education would be accessible to all; but it could create an important opportunity for governments to reorder their budgets.

## How large is the debt problem?

- By 1998, developing countries owed US\$2200 billion (=US\$2.2 trillion).
- By 1998, sub-Saharan Africa alone owed US\$222 billion, or 71% of its annual output.
- Countries like Ethiopia and Mozambique spend a third or more of their export earnings servicing their debt (see table).
- In 1994, actual debt service payments were roughly half of those scheduled.<sup>3</sup>
- For every \$1 in overseas aid from wealthy countries to developing countries, \$13 returns in debt repayments (1999).

The World Bank has identified 41 Heavily Indebted Poor Countries (HIPC), which are so indebted that it is very unlikely they will ever earn enough to repay their debt.

## How did the debt crisis come about?

In the 1970s and 1980s, developing countries borrowed large sums of money. Western banks were only too willing to lend to increase their profits. The money was used partly for social and economic development after years of colonial rule, partly to pay for oil (whose price increased sharply in 1972-3 and in 1979) and partly for more questionable purposes such as military equipment, grandiose constructions and personal luxuries. Neither the borrowers nor the lenders paid much attention to how well the loans would be used or whether they could be repaid.

Meanwhile, developing countries were encouraged to improve their economies by growing cash crops for export. While production increased, agricultural prices fell (but the prices of oil, used in fertiliser and machinery, and manufactured goods did not), so countries did not earn enough to meet their debt repayments. They had to borrow more than ever just to pay the interest.

The situation became critical in 1982 when Mexico, a major debtor country, announced it could not repay its debts. The World Bank and the International Monetary Fund (IMF), intergovernmental agencies related to the United Nations, stepped in with new loans to "rescue" Mexico. Their loans were issued under strict conditions - known as structural adjustment programs (SAPs) [see box].

As other countries found themselves in similar difficulties, they had to accept loans on conditions imposed by the IMF and the World Bank. Debts were often "rescheduled" - that is, debtor countries were given longer to repay. But this simply meant more instalments, without the debt being wiped off. New loans often went towards interest payments, instead of enabling countries to build infrastructure (roads, bridges, telecommunications) or provide essential services such as healthcare and education. The environment suffered, as developers were allowed to exploit forests and fishing grounds to earn much needed foreign exchange.

**Hardest hit:** some facts and figures about selected Heavily Indebted Poor Countries

Country	Population (millions, 1996)	National income per person (GNP) (US\$, 1996)	Debt per person, (US\$, 1996)	Total debt (\$US millions, 1996)	Debt as % of annual GNP	Debt service as % of the total value of exports (1996)
Mozambique	18	80	324	5842	411	32.3
Nicaragua	5	380	1185	5929	322	24.2
Ethiopia	58	100	173	10,077	149	42.2
Zambia	9	360	790	7113	161	24.6
Bolivia	8	830	647	5174	57	30.9
Uganda	20	300	183	3674	32	20.0

Sources of data: 1998 World Development Indicators pp 12-14, 238-40, 242-44

## Structural adjustment programs

How they're supposed to work	But there can be problems
Governments cut spending, to balance their budget and increase investor confidence.	Public sector job losses contribute to increased unemployment and poverty, and sometimes to migration by skilled workers.
Users pay for services, so they're not a drain on the government budget.	Many poor families have no money to spare for education and health. The economic cost of poor health and illiteracy is considerable.
Governments remove subsidies, so prices will find their own level according to the market.	Sharp increases in basic food prices hit the poor hardest, and may lead to violent protest.
Governments devalue currency, to discourage imports and stimulate exports.	The well-off can still afford imported luxuries, but small businesses cannot afford to import machinery and spare parts.
Governments encourage farmers to grow cash to earn foreign exchange.	Food-producing land is used for other crops, so families no longer grow their own food
Utilities and state corporations are privatised to increase competition and cost-effectiveness.	Control of essential services may pass to foreign owners, and many jobs may be lost.
Tax systems are reformed, both to increase revenue and to share the burden more equitably.	Some taxes hit the poor hardest, while the rich are able to evade payment.

# How is the debt problem being tackled?

Many countries have agreed to implement structural adjustment programs in order to receive further loans, in the hope of eventually paying their debt. Some countries have benefited from debt conversions by which creditors or donors allow them to pay instead for development and environment projects - but such swaps involve only a small share of the total debt.<sup>4</sup> A wider reaching strategy has been the Brady Plan (named after the US Treasury Secretary) by which many Latin American countries "sold" their debt at reduced price as investment bonds.

By the mid-1990s, it was widely agreed that many countries, especially in Africa, had no prospect of being able to repay.

## The HIPC Initiative

In 1996, the World Bank and the IMF produced a proposal for debt relief (supposed to ease the pressure of debt) which was more comprehensive and looked more promising than previous attempts to address the debt problem. This "HIPC Initiative"

- allowed for systematic involvement by all creditors
- for the first time, allowed for the reduction of debts owed to multilateral institutions (e.g. the IMF and the World Bank)
- aimed to enable countries to exit from "unsustainable" debt burdens.

However, to qualify under this scheme, countries have to demonstrate a track record of implementing structural adjustment reforms over six years. This means that only a handful of countries (including Uganda, Bolivia, Mozambique) will receive debt relief before the year 2000. Others may have to wait much longer, while their poorest citizens pay the price for delay. Less than one-tenth of the total debt of the 41 poorest countries will be tackled, while their debt service payments continue to rise and prices for their agricultural exports continue to fall.

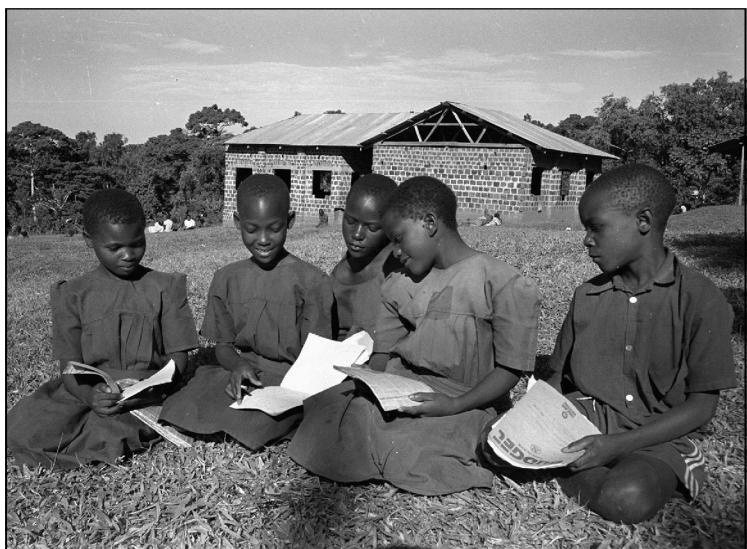
Many observers say that the HIPC Initiative, though well-meaning, is too little, too late, and punishes only the borrower. Each year that countries have to meet excessive debt repayments, they are less able to improve services. For Mozambique, debt relief promised under HIPC will provide only US\$13 million savings in debt service per year - less than US\$1 per person. In 1999, the HIPC process is being reviewed. It seems likely that creditor nations will agree to significant concessions.

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## Debt and World Vision

As a non-government development agency, World Vision works in many of the world's heavily indebted countries, and among many communities who miss out on essential services because of their national debt. Often, World Vision projects assist people to obtain services for which there are insufficient government funds. Thus World Vision has helped to rebuild health clinics in remote rural areas of post-war Mozambique, and to train local health workers to recognise and treat simple illnesses. In Kenya, young people who have left school without job qualifications are undertaking training as carpenters, hairdressers and printers. Through micro-credit initiatives, World Vision also encourages communities to invest local resources productively in small businesses such as food stalls and trade workshops.

World Vision also recognises the importance of action to deal with debt by governments and international financial institutions. Such action should be based on transparent, responsible decision-making and mutual accountability, paying special attention to the impact of policy on the poor.



World Vision has helped these students in Uganda to gain an education.

# Jubilee 2000 - the promise of debt cancellation

The Jubilee 2000 campaign is a growing movement of organisations and individuals, calling for the *unpayable* debts of heavily indebted poor countries - estimated to total less than US \$300 billion - to be cancelled by 31 December 2000. Supporters are lobbying politicians, especially in industrialised countries, to pledge their governments' support. The campaign collected over 17 million signatures for a massive petition, presented to the leaders of the G8 countries (Germany, France, USA, Canada, UK, Russia, Italy and Japan) at their summit in June 1999. These nations are owed most of the government debt, and are also major shareholders in the IMF and World Bank. Jubilee 2000 argues that debt relief should be granted on a case by case basis and closely linked to borrowers' undertaking to spend the money saved on agreed strategies to reduce poverty.

## Debt matters

Unless action is taken to deal with chronic indebtedness and its causes, the whole world will suffer the consequences of indebtedness: job losses as poor countries cannot afford imports, increased migration as people seek to escape poverty, global warming and loss of bio-diversity as tropical forests are cleared, the problems of the drug trade on which some indebted countries rely for income - and the increased danger of conflict resulting from the gap between rich and poor.

In order to guard against further crippling debts, debtors and creditors should take responsibility for the terms of future borrowing. This would involve

- appropriate interest terms, according to the purpose of the loans
- developing export sectors so that repayments would be affordable

Dealing with indebtedness will not on its own bring about an end to poverty. However it could make a big difference to the capacity of governments to provide for the well-being of their citizens. Also the attitude of shared responsibility that is represented could signal an important step towards a world that no longer accepts that poverty is inevitable.

## Notes on sources

This topic sheet draws on reports and photos from WV colleagues in Nicaragua, Mozambique, Kenya and Uganda, as well as Jubilee 2000 resources.

1 Emma Curtis, *Child health and the International Monetary Fund: the Nicaraguan experience* on [www.jubilee2000uk.org/features/health0801.html](http://www.jubilee2000uk.org/features/health0801.html)

2 Larry Elliott, "Dealing with the debt gods" in *Guardian* special feature on debt May 15 1998

3 *World Debt Tables 1996* vol 1 p 37

4 *Reality of aid 1997-8*, p 223

Compiled by Deborah Patterson  
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The cost of cancelling unpayable debt is not as great as people might expect. Private banks have already written off some loans that they do not expect to be repaid, and borrowers have repaid more than the original debt. Cancelling debts owed to governments and bodies such as the World Bank *would* involve writing off some assets - and therefore some loss of income - or would require increased contributions by member countries. However the cost has been calculated to be less than 0.2% of the world's GNP for one year, equal to a slight slowing in economic growth. While some critics argue that debt cancellation will damage debtor countries' credit rating for future borrowing, heavily indebted countries effectively have no credit rating to lose. Since industrialised countries have responded so quickly with more than US\$100 billion to the Asian economic crisis, surely it is possible to deal justly with chronically indebted countries.

## Action you can take

- **Find** out more about how debt affects people such as farmers and small business operators in Australia. What laws are there to protect borrowers or lenders? Do they seem to favour the well-off or the poor?
- **Read** about the concept of Jubilee in the Bible, especially in Leviticus 25. (Jesus referred to the Jubilee when he read from Isaiah in the synagogue in Nazareth, Luke 4)  
**Reflect:** What was the purpose of the Jubilee year? How do you think modern readers should understand this passage?
- **Order** the latest Jubilee 2000 (Australia) resources (including campaign updates), and use them to inform your friends, class or church about the issue of debt. Keep in touch with the debt issue by checking the Web at [www.jubilee2000uk.org](http://www.jubilee2000uk.org)
- **Write** letters to political leaders. Obtain letter-writing guidelines from World Vision Australia or other coalition members.
- **Support** World Vision projects assisting communities with water supply, housing, health care and education - and low-interest loan schemes to help people avoid extortionate interest rates.

## World Vision resources on related issues include

"As we forgive our debtors" *Grid Extra*, Summer 1997/8 - 4 pages, includes an outline of the Biblical model of Jubilee

"Breaking the chains: debt" in *Action News*, Spring 1998

**Useful web sites** include the Jubilee 2000 site at [www.jubilee2000uk.org](http://www.jubilee2000uk.org)

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