

# Enough is enough: The debt repudiation option



We believe in life before death

**Front cover photo:** Mine workers at Chibishi mines in Zambia usually work eight-hour shifts, but many work overtime, pushing their time underground to 16 hours a day

**Photo:** Christian Aid/David Rose

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## Introduction

The dust is settling on the huge Make Poverty History mobilisation of 2005, and the debt cancellation deals announced amid so much fanfare are finally being signed. But how much has really been done to provide poor countries with the 'sustainable exit' from debt crisis promised by rich country creditors more than ten years ago?

The answer is that a select few of the world's poorest countries – around 20 – have received substantial debt cancellation (although some of them countries still face real debt difficulties). But most countries have received little or no debt cancellation, and many face even worse debt problems now than they did a decade ago.

In September 2005, Christian Aid published a report heralding a new era of debt campaigning, entitled *What About Us? Debt and the Countries the G8 Left Behind*. We called for a fair and transparent arbitration process through which countries could reach a fair resolution to years of debt bondage, taking full account of odious debt and the harmful role lenders often play in the build-up of debt. We stand by those recommendations and urge the international community to take them forward.

But we also recognise that the need to deal with the debt remains urgent. Increasing numbers of analysts and campaigners, including the influential economist Jeffrey Sachs, are calling for countries to consider simply not paying all or part of their debt obligations in order to spend money on vital services. In this briefing, Christian Aid supports that call.

In the first two sections of this paper we demonstrate that debt remains one of the main barriers to development in many of the world's poorest countries, and in many so-called middle-income countries (MICs). We argue that much of that debt is illegitimate. This fact is increasingly recognised as important and lends much weight to the idea of repudiation.

The rest of this paper argues that it may well be in poor people's interests for their governments to repudiate debt. So far, debates about debt repudiation as a genuine, moral and positive option for debtor countries have been dominated by threats from creditors. Countries that have chosen in the past to repudiate or default on all or part of their debt have sometimes been 'punished' by creditors and potential future financiers. They have found that their financing, especially concessional financing, has been cut off; diplomatic relations have turned frosty; and assets held abroad have even been seized. Countries considering non-payment are warned **by creditors** that they will be ostracised from the global financial market.

But there are strong reasons to suspect that such costs of repudiation have been exaggerated. In reality, private investment arrives when it can reasonably expect a decent return. Investors are not very interested in 'punishing' countries. And although it is real, the threat of becoming politically ostracised is less dangerous in a world where rich countries face electoral pressure if they are seen to be acting against the interests of poor countries.

Repudiation still comes at a cost and needs to be treated very seriously. However, its benefits seem to have been overwhelmingly ignored. Advice from creditors, such as the World Bank and the International Monetary Fund (IMF), is increasingly accepted as

having had disastrous consequences on a range of issues. These range from rapid liberalisation and privatisation to reducing capital controls and charging fees for education and health. Creditors' views on the issue of non-payment of debts are equally self-serving and one-sided.

Reserving the money currently being spent on servicing debt for education and health and other urgent needs has clear social benefits. Countries with major debt problems often pay more to service their debt than on basic services. People's lives can be saved and improved in the short term if more money is quickly diverted from debt payments to meet their needs.

But the simple economic benefits of debt repudiation are the most overlooked. Yes, there is a price for refusing to pay one's debts – an exaggerated price maybe, but a price nevertheless. But having a generation of young people who lack an education also comes at a price, as does having an unhealthy workforce that lacks access to medical treatment, and millions of children who have been orphaned by HIV. Lacking an infrastructure that can promote the domestic and export market comes at a high price. How can economic prosperity be built on such foundations?

It is time for economists and politicians in all countries to weigh up the real pros and cons of non-payment, and act in the interests of citizens instead of powerful financial institutions.

Not all governments should be encouraged to repudiate. If a government does not pursue a pro-poor agenda, debt repudiation – just like traditional debt relief, aid or any type of funding – may not lead to positive outcomes for poor people. But within the context of a pro-poor development plan, repudiation should be taken seriously as a realistic option.

But even when repudiation is not the right option, opening up a debate about repudiation is still the right way forward for debt campaigners and developing-country governments. The issue of illegitimacy is paramount. How long will the self-serving myth persist that lenders are exempt from blame? To counter it, debt audit processes are springing up throughout the developing world as citizens seek to find out the truth about the debt burdens blocking their development. As these audits uncover the secrecy, failure and often criminality surrounding loans, calls for repudiation are bound to grow. By exposing the history of loans and debt accumulation, such processes will lead to greater accountability of governments to their parliaments and people.

### **Journey to repudiation**

<b>1982</b>	Mexico's threatened default marks start of modern debt crisis
<b>Early 1990s</b>	The Debt Crisis Network builds support in the UK for a radical approach to eliminating the debt burden
<b>1996</b>	The Highly Indebted Poor Countries (HIPC) initiative is launched, but this latest attempt to deal with the debt crisis for the poorest countries is too narrow in its scope
<b>1997</b>	The Jubilee 2000 movement is founded; Christian Aid is a leading founding member
<b>1998</b>	Birmingham G8 meeting sees massive human chain – a day of hope
<b>1999</b>	The Enhanced HIPC initiative offers substantial debt cancellation for countries fulfilling strict criteria

<b>July 2005</b>	Nine years since the start of the HIPC initiative, only 19 countries have qualified for debt relief. The Gleneagles G8 offers some more debt relief to a handful of countries. Campaigners hail limited victory
<b>September 2005</b>	Christian Aid publishes <i>What about us? Debt and the Countries the G8 Left Behind</i> , laying out a bold vision for a sustainable end to debt domination, emphasising creditor responsibility
<b>October 2005</b>	Campaigners from around the world meet in Havana, Cuba, to plan next steps in the campaign
<b>January 2006</b>	UK chancellor Gordon Brown calls for 'full debt relief' for 'all the world's poorest countries'
<b>June 2006</b>	Christian Aid sponsors global conference on debt repudiation in Nairobi, Kenya
<b>January 2007</b>	Christian Aid calls on countries to repudiate their debts when doing so will lead to vital improvements in basic service delivery

In the report *What About Us?* we stated that if developing countries wait for creditors to cancel their debts, they could be waiting a long time. We have had no reason to re-evaluate that assessment since 2005. It is time for debtor countries to take the initiative in the interests of their people. It is time for the weak to stand up to the strong. It is time, for some countries, to repudiate their debt.

## Section 1: Is there still a debt crisis?

In recent years creditor governments have given the impression, quite successfully, that the debt crisis against which the world rose up in horror in the 1990s has been dealt with generously and comprehensively. But has it?

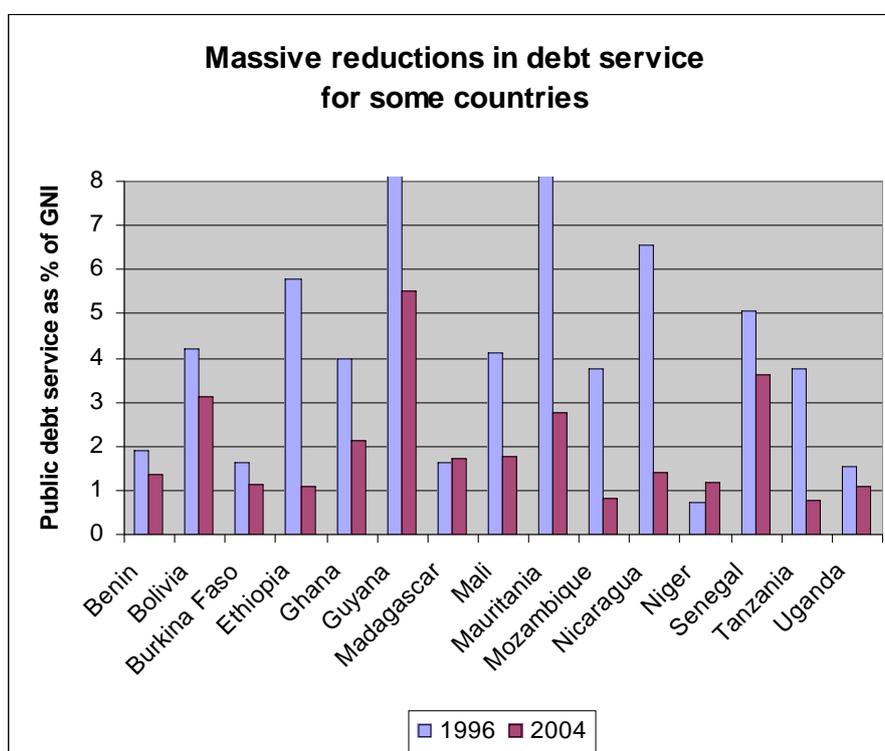
Research published by Christian Aid, ActionAid and the UK's Jubilee Debt Campaign in 2005 demonstrated that at least **60** countries needed total debt cancellation in order to meet the millennium development goals.<sup>1</sup> In January 2006, the UK's chancellor Gordon Brown appeared to agree when he called for full debt relief for the **66** countries considered eligible for concessional lending from the World Bank.<sup>2</sup>

These assessments of the scale of required debt relief contrast with what has actually been done. Since 1996, when developed country governments first started promising a 'sustainable exit from debt crisis', just **20** countries have received significant debt relief under the HIPC initiative.<sup>3</sup> The rest are still waiting. And still paying.

Huge debts also continue to devastate the economies of some of the world's MICs, such as Indonesia, the Philippines, Peru and Ecuador. These need to be dealt with too in a fair and generous way.

### The select few

The 20 countries that have benefited from the comprehensive debt relief promised when the HIPC initiative emerged a decade ago are known as the completion point HIPCs. They have passed all the conditions set by creditors to grant debt relief.

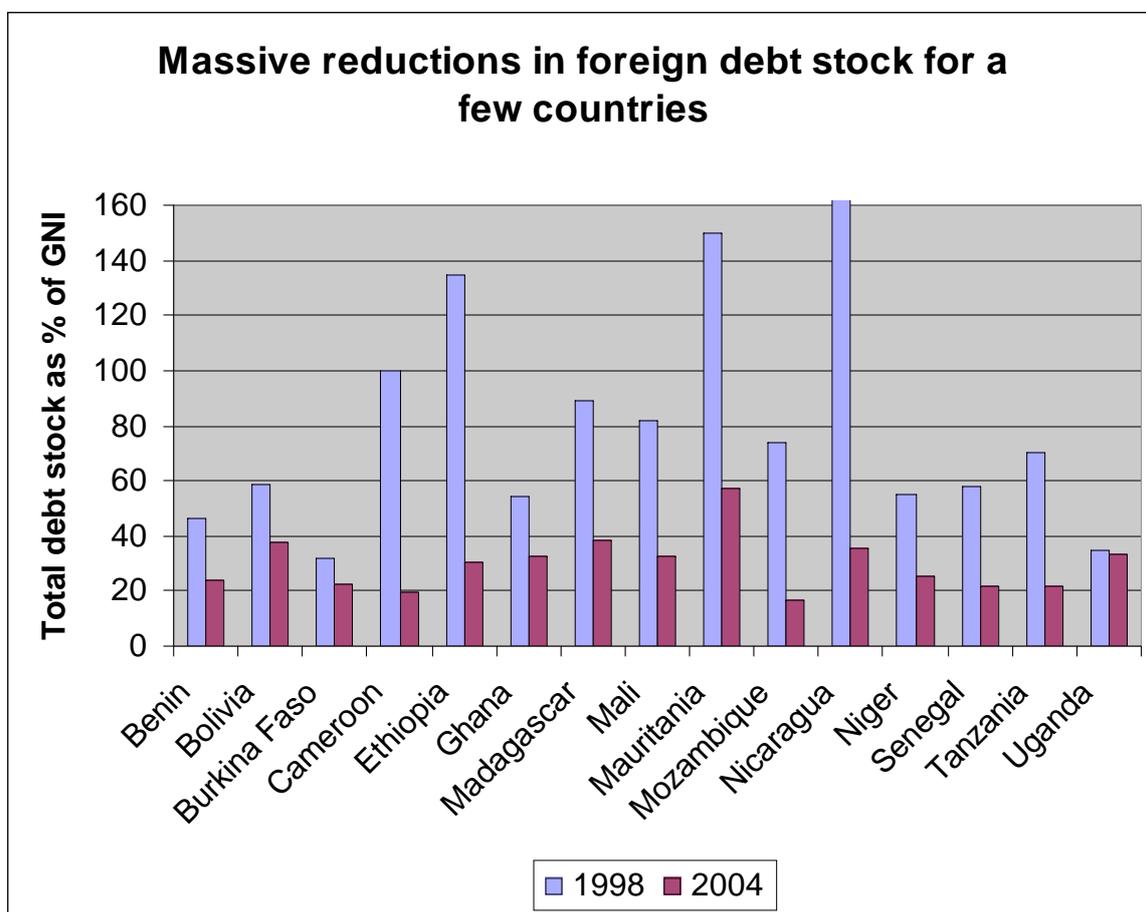


Completion point countries' external debt service payments had been significantly reduced by the end of 2004, the year for which the most recent data are available (see table above).<sup>4</sup> The situation has improved further since the Gleneagles deal in July 2005, when a large amount of multilateral debt was cancelled. Multilateral creditors were

by far the largest group of remaining creditors for completion point HIPC in 2005, receiving on average 62 per cent of these countries' foreign debt service.

One of the facts that shocked the world in the 1990s was that many of the world's poorest governments were paying more to service their debt than on healthcare for their people. From the limited figures available (the most recent are from 2003) it appears that debt cancellation has made a real difference. Only two out of the nine countries that had received debt cancellation by the end of 2003 were still paying more to service their debt than on health services, compared with five in 1998 (the earliest year with records). All nine countries had improved the ratio of debt versus healthcare spending.

Completion point HIPCs have also seen large reductions in their debt stock. According to new Christian Aid data, nine of the 15 countries that had passed the HIPC Completion point by the end of 2004 had seen more than a 60 per cent reduction in their stock of external debt (Net Present Value (NPV) as a percentage of Gross National Income (GNI)) since 1998. A further four had seen a reduction of more than 40 per cent. All had seen their debt stock reduce.



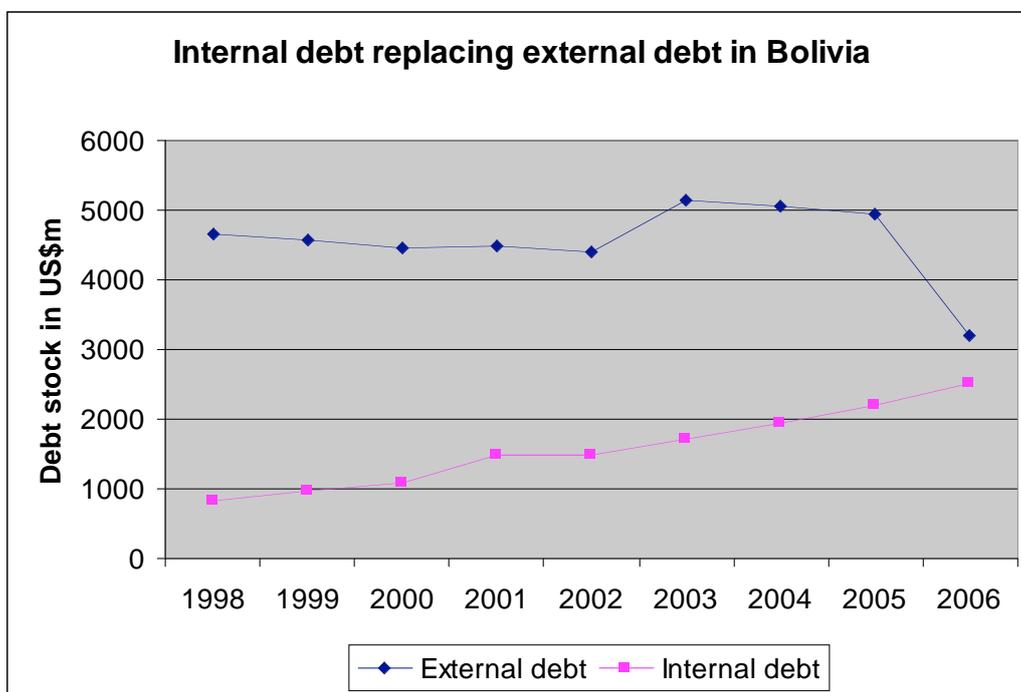
However, even for these select few, the promise of a sustainable exit from debt crisis remains elusive. A combination of new borrowing, falling export earnings and unfavourable exchange rates has caused their foreign debt burdens to rise again. According to an analysis carried out by the World Bank's Independent Evaluation Group in 2006, the debt burdens of 11 of the 13 completion point HIPCs for which they had data had increased since they passed completion point. In eight of these countries the ratio of debts to exports, the key criteria upon which debt sustainability is judged in the HIPC initiative, are back above the 'unsustainable' level.<sup>5</sup>

In addition comes the increasing problem of domestic or internal debt (see box below). While accessible data on domestic debt is hard to come by, it is clear that domestic borrowing is filling the gap in many countries that are seeing a reduction in their foreign debt. Official 'debt sustainability' assessments do not presently take internal debt into account.

### Internal debt

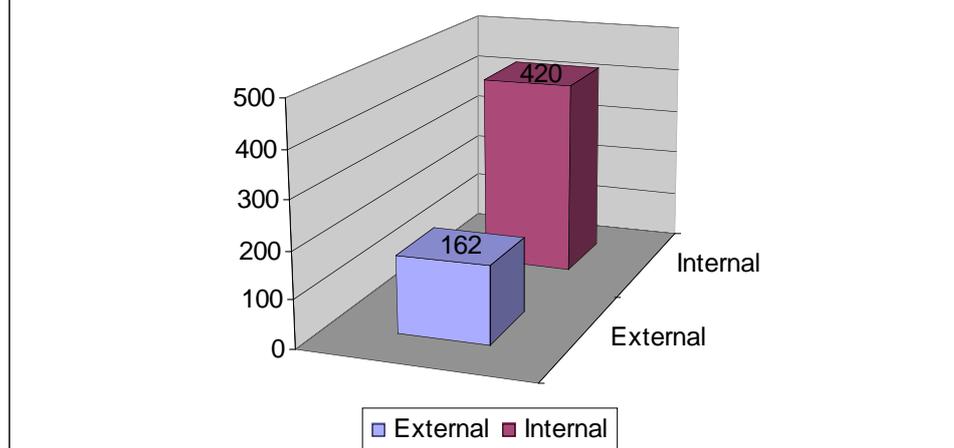
The completion point HIPC's external debt burdens have decreased significantly, both in terms of stock and servicing. However, some countries are seeing a worrying increase in internal debts, which are often taken on to pay off external debt.

Bolivia, for example, as an early member of the completion point HIPC club, has seen its external debts dramatically decline since the mid-1990s. But every dollar lost from its external debt burden has been replaced by another dollar of domestic debt, which is more expensive to service because interest rates are higher.



In 1998, as it joined the HIPC process, Bolivia owed US\$4.6bn in external debt, and only US\$800m domestically. By 2006, its external debt had dropped to US\$3.2bn, but its internal debt had risen to US\$2.5bn. In total, Bolivia owed US\$5.4bn in 1998 and US\$5.7bn in 2006.

### Internal v external debt service in Bolivia (US\$m)



Internal debt can often be little more than external debt by another name. When a government sells bonds in the country's own currency and in domestic markets, the debt is called 'internal'. But as these bonds can be sold to international investors, it is quite feasible for a country's entire stock of supposedly internal debt to be owed to investors abroad. In effect, the leakage of money from the country can continue unabated.

Perhaps most importantly, the impacts of the conditions attached to HIPC debt relief have led to serious economic difficulties in many of the completion point HIPCs. In some cases the negative impacts of the conditions, such as privatisation and trade liberalisation, have quite possibly outweighed the positive impacts of partial debt cancellation.

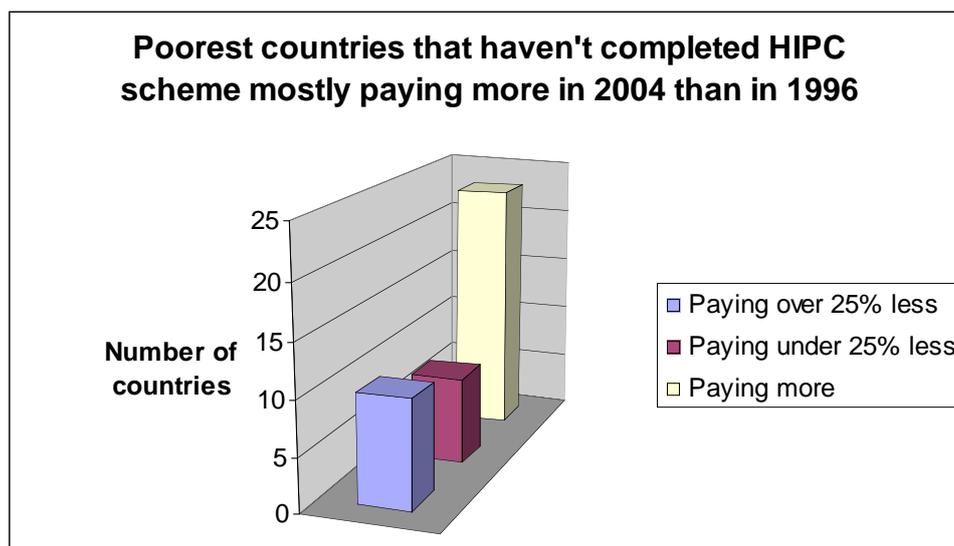
### All other countries

#### *i) Low-income countries*

Since 1996, the governments of the world's poorest 66 countries have paid a total of more than US\$230bn between them to service their foreign debt. This far exceeds the grants they have received from donor countries. Had this money been spent on healthcare, education and infrastructure, the millennium development goals – which today seem like a fantasy – might have been within the world's grasp.

In 1996, most of the world's poorest countries were in debt crisis. Christian Aid's analysis shows that this is still the case for many of them, and the continuing refusal of the developed countries to deal with the situation remains a scandal.

A decade on, we have data for 41 low-income countries that still do not fulfil creditors' conditions for HIPC debt relief. Only ten of these countries have seen their annual payments on foreign debt decrease by more than 25 per cent; 23 are paying more on debt servicing now as a percentage of gross national income (GNI) than they were in 1996; and for an other eight countries, payments have decreased by less than 25 per cent.



When we look at the present value of the debt stock, 15 of the 41 countries have seen a reduction of more than 25 per cent in their debt stocks compared to GNI. Of the remainder, 12 have seen increases and the other 12 have seen small reductions of less than 25 per cent.

Completion point HIPC's now mostly pay more on healthcare than on servicing their debts. In contrast, 25 of the remaining 50 countries that receive concessional lending from the World Bank for which we have figures spent more on debt servicing than on health in 2003. This is down from 30 in 1998. For 16 countries, the ratio between healthcare and debt servicing had worsened.<sup>6</sup>

#### *ii) Other poor countries*

It is not only the low-income countries that face problems with continuing and increasing debt burdens. Many MICs also face debt problems. Peru, Jamaica and the Philippines were among those included in the original list drawn up by the Jubilee 2000 campaign of countries requiring debt cancellation. But others are also in desperate trouble. Some, such as Ecuador, Indonesia, Argentina, Kazakhstan and Brazil, were classified as 'severely indebted' by the World Bank itself in 2005.

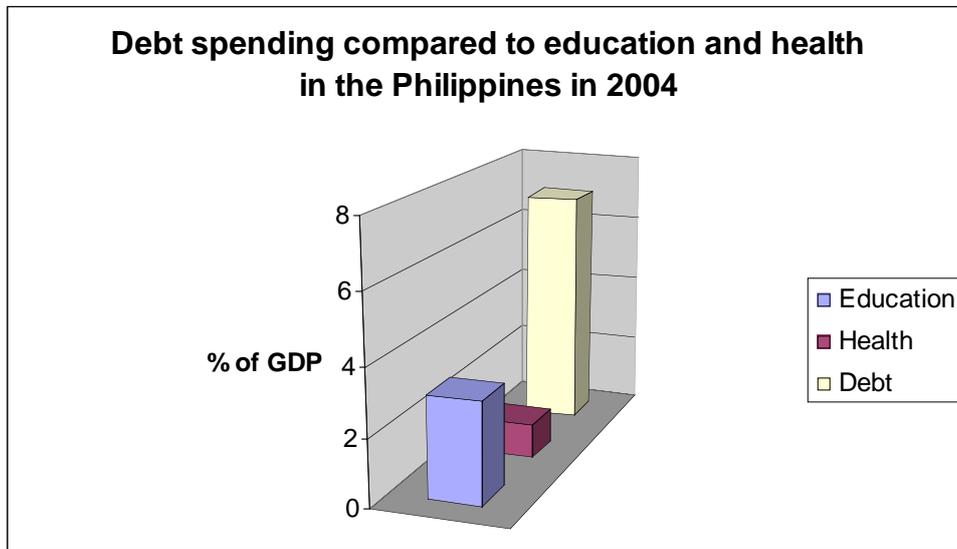
More than a billion people in MICs live on less than £1 a day.<sup>7</sup> It has become commonly accepted in official circles that there can be no significant debt cancellation for MICs. But this analysis ignores the extent to which debt is holding back development in these countries, and the vast quantities of illegitimate debt that should be cancelled immediately.

#### **Philippines – an unsustainable burden**

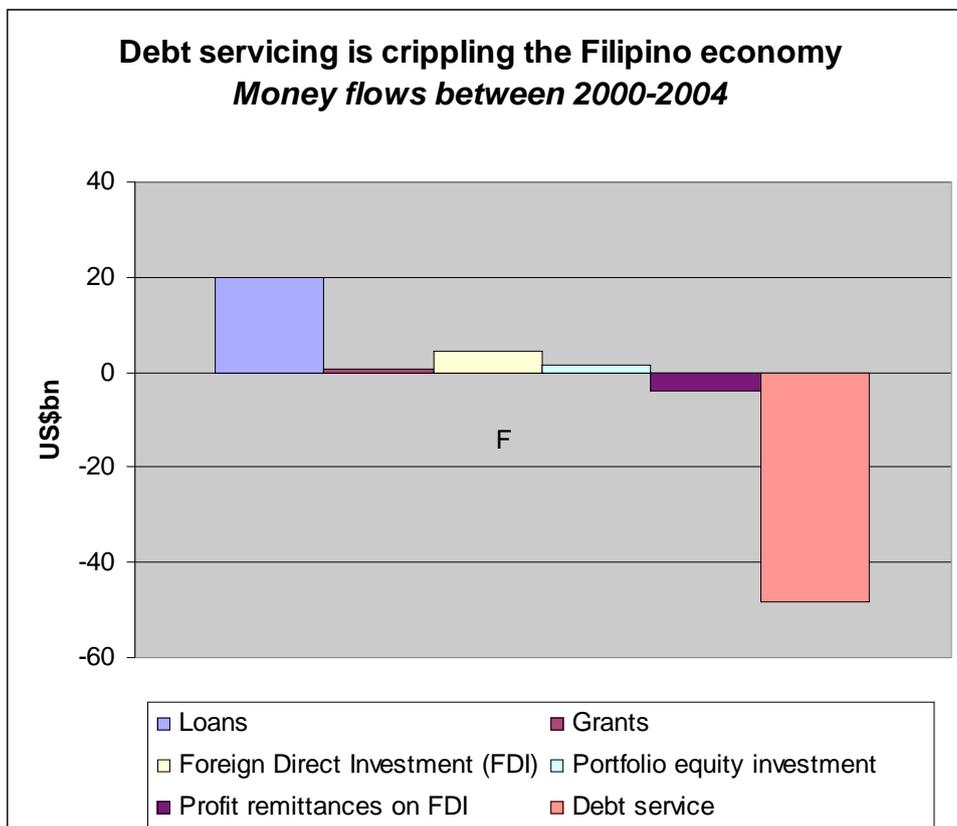
Poverty has been on the rise in the Philippines. The percentage of the population living on less than US\$2 a day rose from 45 per cent in 1997 to 47 per cent, or 38 million people, in 2000 (the last year with available data). General unemployment has increased from eight per cent in 1995 to ten per cent in 2002, while unemployment among young people rose from 16 per cent to 26 per cent in roughly the same period.

In the face of these worrying indicators, has the government increased its spending on basic services? No. Public spending on healthcare has fallen from around two per cent of GDP in the 1990s to around one per cent in 2004, while education spending has fallen from four to three per cent. In stark comparison, the government has spent seven

per cent of the country's GDP on servicing its foreign debt. In 2004, debt repayments constituted 31 per cent of the Philippines' national budget – more than it spent on all its social services combined.



The Philippines' service payments increased from US\$4.25bn a year in 1995 to almost US\$7bn in 2004, and since 2000 the country has haemorrhaged more than \$48bn in debt payments compared to new loans of under US\$20bn (see graph below). But these crippling payments have not led to a reduction in the Philippines' huge debt burden – external public debt rose from US\$28.5bn in 1995 to US\$35.5bn in 2004. Taking into account private debt, the Philippines now owes its creditors much more than US\$60bn.<sup>8</sup>



Gloria Arroyo, president of the Philippines since 2001, admitted in 2004 that her country is going through a debt crisis, raising fears of a sovereign default among creditors.<sup>9</sup> But the government's stance on debt continues to be an accommodating one. Worried that access to foreign capital would dry up if it simply refused to pay part or all of its debt, no Filipino government has seriously considered taking such action.

The country's automatic appropriation law currently prioritises resources for debt repayment regardless of how much money there is in the budget. This means that debt does not appear in the budget and congress has no chance of scrutinising it. Government expenditure on services such as healthcare and education is therefore much lower in relation to the total allocation of resources than what is reflected in the budget.

But Christian Aid's partners in the Philippines are calling for this situation to be reversed. These campaigners want social spending to be prioritised and a clear ceiling set on debt servicing. As Lidy Nacpil, of the Freedom from Debt Coalition, in an interview with Christian Aid, said: 'It is time to listen to our people's stories. It is time for their cries for justice to be heard.'

Pressure groups are also calling for an official national audit of the country's debt to be carried out by congress representatives, with civil society participation. The House of Representatives approved the proposal for an official audit in September 2004, but it is currently stalled in the Senate. In the meantime, the Freedom from Debt Coalition is already organising the Citizen Debt Audit with the participation of a range of experts, including lawyers, public accountants, doctors, trade union and NGO leaders and former government officials. Once the information has been gathered, the committee can assess legitimate and payable debt against illegitimate and unpayable debt.

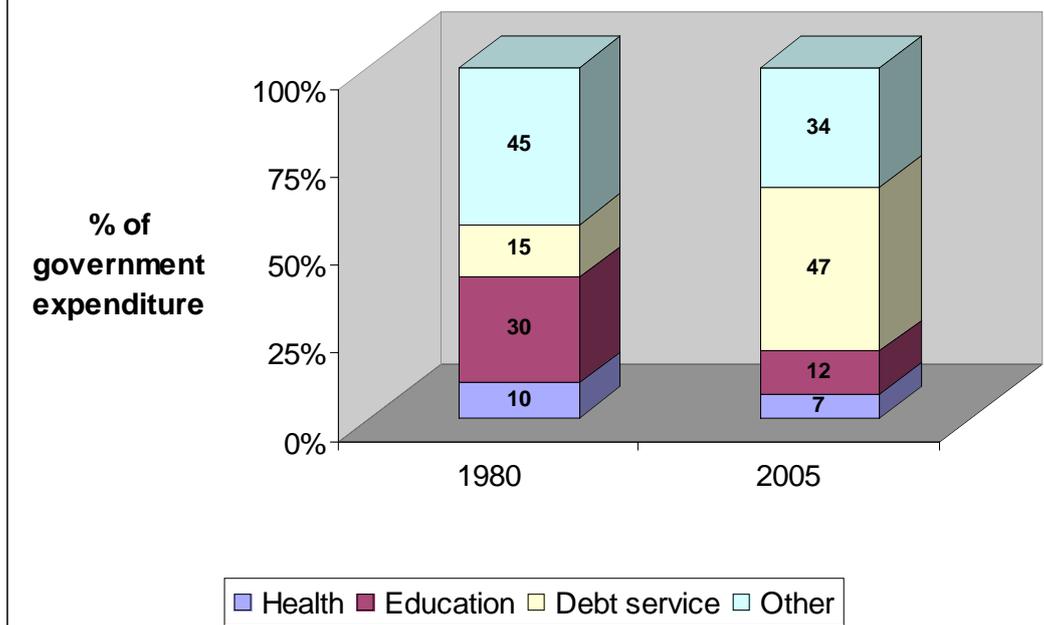
Whatever measures the Philippines adopts in relation to its outstanding debt, it must review its borrowing policies to avoid accumulating unsustainable debt again. It also needs a longer-term vision for building up domestic capital – for example, by reviewing its tax policies. There is a strong case for abolishing the tax breaks and holidays that the government currently grants foreign companies to attract inward investment. However, such a move would require solidarity across the region to prevent foreign companies from moving on to those countries where regulation is weakest.

Some MICs have benefited from limited debt cancellation. One of the methods used is a so-called 'debt-for-development swap', whereby official creditors write off debt repayments, as long as these funds are invested in poverty reduction. These schemes should be welcomed if they help countries to spend money on social services rather than debt payments. But to date, such schemes have been on a limited scale and on their own they are unlikely to make substantial inroads into the build-up of debt.

### **Ecuador – forced to choose between debt and social spending**

In 1980, the Ecuadorean government spent 30 per cent of its revenue on education, as well as ten per cent on healthcare and 15 per cent on servicing its debts. By 2005, this situation had been reversed. Today, Ecuador spends 47 per cent of its government income on servicing debt and only 12 and seven per cent respectively on education and healthcare. Meanwhile, poverty has increased – especially in rural areas – from 55 per cent of the population in 1995 to 60 per cent in 2003.<sup>10</sup>

### Debt service replacing social spending in Ecuador



Ecuador has recently made large profits from oil sales. As part of the requirements of an IMF loan programme, the government set up an oil stabilisation fund in 2001 into which its oil revenues would be accumulated. When the Ecuadorian Congress made moves in 2002 to set aside a portion of this fund for social sector spending, the IMF raised objections, arguing that dealing with the country's debt was a priority. Despite this pressure, setting aside ten per cent for health and education was eventually passed into law.<sup>11</sup>

In 2005, Ecuador's then-finance minister Rafael Correa worked alongside Congress to further restructure the oil stabilisation fund in order to channel a greater portion of oil revenues into social sector programmes. This time, both the IMF and World Bank objected. The World Bank delayed and ultimately cancelled an already approved loan to Ecuador, based on their concern that these changes amounted to a 'policy reversal'.

It is absurd and disgraceful that pro-poor and democratic policies are being vetoed by organisations supposedly interested in reducing poverty and democracy.

## Section 2: Illegitimate debt

The simple fact of being in so much debt that it cannot pay for basic services such as healthcare and education gives a country enough of a moral case to consider repudiating its debt. But the case gets even stronger when it becomes clear that much of the debt that poor countries have built up is illegitimate.

More and more countries are carrying out audits of their debt burdens to see what they actually owe, and the truth behind how and why poor countries got into debt is finally emerging. Poor governance in debtor countries is one of many reasons for the debt crisis. Lenders are also to blame.

While there are a variety of opinions on what constitutes illegitimate debt, experts agree on two main areas. These are:

1. odious debts
2. penalties and exorbitant interest rates.

### Illegitimate debt 1: Odious debts

The debts that many democratic countries owe today were often built up by the dictators and tyrants of yesterday. Estimates and ongoing audits suggest that at least 20 per cent of developing country debts (more than US\$500bn) can be described as 'odious'. This means that the original loans were made to corrupt or despotic regimes where the money was likely to go missing.<sup>12</sup> In Christian Aid's view, these debts should not be repaid under any circumstances.

The notion that lenders should always be repaid, regardless of how and to whom they lend, is morally indefensible and economically unsustainable. It is immoral that poor people's taxes and government revenues are spent on paying back loans made to the despots who oppressed them, instead of on social and infrastructural investments.

#### Examples of illegitimate debt<sup>13</sup>

- **Philippines:** When President Ferdinand Marcos went into exile in 1986 he had stashed away between US\$5bn and US\$13bn – up to a third of all the money lent to the country during his dictatorship.
- **Brazil:** The military junta borrowed about US\$100bn between 1964 and 1985. It is unclear what this money was spent on, but much was certainly stolen or used to import luxury goods. In the 1980s, Brazil spent US\$48bn on servicing its debt while its debt stock increased by US\$40bn, demonstrating the exorbitant interest rates of the time.
- **Indonesia:** More than US\$100bn was lent to General Suharto during his 31 years in power.
- **Argentina:** During the military junta's seven years in government between 1976 and 1983, the country's foreign debt rose from US\$8bn to US\$46bn.
- **Haiti:** In exchange for independence from France in the 19th century, Haiti had to pay the equivalent of US\$21bn in today's money. The dictator 'Papa Doc' Duvalier stole around a billion dollars between 1957 and 1971.

- **Kenya:** President Daniel Arap Moi stole an estimated US\$4bn from the Kenyan Treasury between 1978 and 2002.
- **Nigeria:** Sucessive military regimes between 1983 and 1998 racked up debts of US\$14 bn, much of which was simply stolen.

### South Africa

When Nelson Mandela was elected president of South Africa in 1994 he inherited external debts of around US\$20bn, which had been racked up by the apartheid government. Banks based in Germany, Switzerland, the UK and the US were the apartheid regime's main financiers as it struggled through its final years. The IMF itself lent South Africa money until it was prevented from doing so by its board in 1983.

Despite the fact that the loans to the apartheid regime were clearly linked to the oppression of the South African people, creditors used threats to ensure that the African National Congress (ANC) government would repay every penny of it.

Speaking in Southwark Cathedral in April 1997, the Archbishop of Cape Town, Njongonkulu Ndungane said: 'As we approach the new millennium, the time has come to invoke the Doctrine of Odious Debt. In the case of South Africa, its foreign and domestic debt was incurred, by and large, under the apartheid regime, and should (...) be declared odious and written off.'<sup>14</sup>

### Illegitimate power: The Bataan nuclear plant

The Philippines' Baatan nuclear power plant is a classic example of odious debt. It is still costing the cash-strapped government around US\$200,000 *every day* despite never having produced a single watt of energy. The project initiated by the dictator Ferdinand Marcos in 1975 was beset by scandal – Marcos is thought to have received upwards of US\$100 million in kickbacks. It was hugely overpriced, costing three times as much as a similar South Korean plant. Baatan has so far cost the country US\$2.3bn and payments are scheduled to continue until 2018.<sup>15</sup>

As early as 1976, both the International Atomic Energy Agency and the Philippine Atomic Energy Commission discouraged the government from going ahead with the plan. The site chosen for the power plant was prone to earthquakes and surrounded by volcanoes.<sup>16</sup> Despite this, private companies, guaranteed by the US Export Credit Agency, funded the project. According to the Philippine Freedom from Debt Coalition (FDC), a Christian Aid partner organisation, the companies knew that the deal would be profitable, even if the loans were found to be fraudulent and overpriced.<sup>17</sup>

The Bataan power plant fiasco is a striking example of loans that have had no positive outcome for ordinary Filipinos, saddling them instead with the debts of an incompetent and greedy dictator. But it is far from unusual: there are 150 loans like it in the Philippines according to an FDC estimate.<sup>18</sup> In 1990, the FDC studied six fraudulent loans in the Philippines and estimated their combined cost to be between US\$4-6bn.<sup>19</sup>

## **Zaire/Democratic Republic of Congo (DRC)**

In 1980, Erwin Blumenthal, the IMF's representative in Zaire, told his employers that there was 'no (repeat:no) prospect for Zaire's creditors to get their money back in any foreseeable future'.<sup>20</sup>

At the time, Zaire was ruled by Mobutu Sese Seko, who amassed a fortune of more than US\$10bn by stealing from his country. When Blumenthal filed his report, Zaire's debt was US\$5bn; by the time Mobutu was overthrown and died in 1998, the debt stood at more than US\$13bn. In the decade that followed Blumenthal's report, the IMF and the World Bank, alongside the British and American governments, lent Mobutu's regime US\$8.5bn.<sup>21</sup> Commercial banks, meanwhile, refused to lend Mobutu more money during that period.

Today, the DRC is one of the world's poorest countries and ridden by conflict. But the world community has never acknowledged that the country's debt should be cancelled because so much of it was simply stolen.<sup>22</sup>

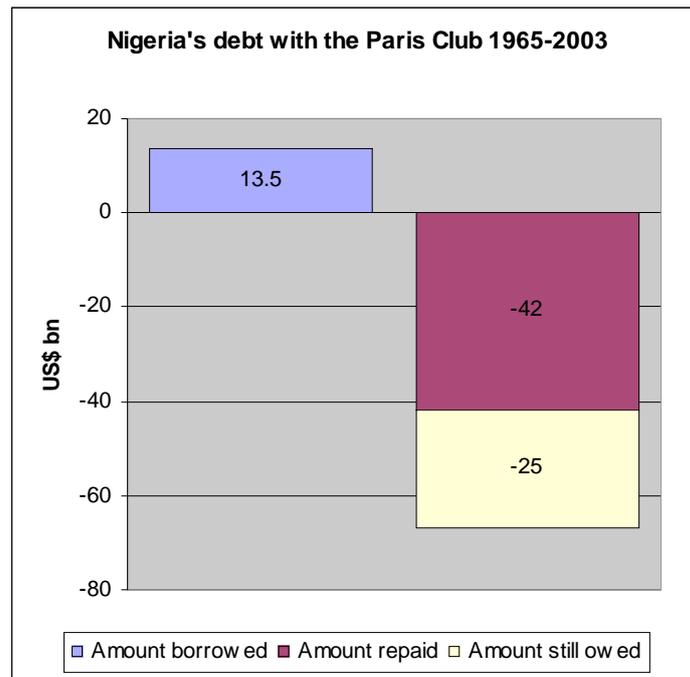
## **Illegitimate debt 2: Penalties and exorbitant interest rates**

Debt builds up when it is not paid on time because creditors charge interest on the arrears and impose financial penalties for late payments. Creditors do not need to do this – they choose to. They therefore have to take responsibility for the fact that their imposed interest rates and penalties have played a part in creating the current debt crisis.

According to a study by the United Nations Conference on Trade and Development (UNCTAD), Africa received \$540bn in loans between 1970 and 2002, and paid back US\$550bn. But because of imposed arrears, accumulated interest and penalties, in 2002 the continent still owed US\$295bn.<sup>23</sup> While it is normal to pay back more than you borrow – we all pay interest on loans – the poorest countries in the world are supposed to receive 'concessional' financing, or very good terms on their loans. The reality for many, however, has been the very opposite.

Nigeria is a good example of the trend. Before a democratic regime was elected in 1999, Nigerian dictators had stopped repaying the debt, accumulating large arrears. Interest on these arrears and large penalties for non-payment constitute the main reason why Nigeria's debt has ballooned so uncontrollably.

In fact, although Nigeria only borrowed US\$13.5bn from Paris Club creditors between 1965 and 2003, it has paid back about US\$42bn because of penalties and interest accrued. Amazingly, Nigeria still had US\$25bn to pay in 2003. In 2000, almost half of Nigeria's debt to the Paris Club was made up of interest on arrears and penalties.<sup>24</sup>



Nigeria's president, Olusegun Obasanjo, is outspoken on this issue. In November 2004 he said: 'To put it bluntly, penalties and interests and all sorts of questionable rescheduling are strangulating our economies and people.'<sup>25</sup> A recent debt deal has seen Nigeria's external debt virtually eliminated through a combination of early payment and cancellation (see pages 28-29 for more details).

### Unfair trade rules

The unfair global trade regime that protects developed countries' agriculture and industry has deepened developing countries' indebtedness and destroyed any chance of repaying their debts.<sup>26</sup> The United Nations believes that unfair trade rules deny developing countries more than US\$700bn every year.<sup>27</sup>

Developed countries have used tariffs and quotas to prevent the developing world from freely exporting their goods. Getting rid of these trade barriers would raise the export earnings of developing countries by US\$100bn every year, according to World Bank estimates.

Analysis commissioned by Christian Aid has shown that the trade liberalisation forced on sub-Saharan Africa as part of structural adjustment programmes in the 1980s and 1990s lost the region US\$272bn in earnings over the last 20 years.<sup>28</sup> This amount would have repaid all of sub-Saharan Africa's debts, leaving enough to put all its children through school.

Trade rules deliberately implemented by developed nations have prevented developing countries from earning enough money to pay off their debts. Many poor people have paid with their lives instead.

Some loans are made in good faith and with positive intentions, but are still imprudent on the part of the lender and should therefore be considered illegitimate. Lending to companies that go bust and cannot repay rightly implies a certain amount of imprudence on behalf of the lender, who must shoulder some of the burden. But states cannot go bust and their debts must always be repaid in full. This is not acceptable. In many cases

grants would have been more appropriate than loans for the poorest countries. As Joseph Hanlon, an expert on illegitimate debt, says: 'Lending money to a starving woman to buy food when she has no capacity to repay does not create a legitimate debt'.<sup>29</sup>

### Section 3: The case for repudiation

Debt payments of often questionable legitimacy are still causing the world's poor people untold harm. What should developing countries do to protect their people? Ideally, an agreement could be reached with creditors to resolve debt crises in a humane way. The debt crisis could be solved quickly if creditors acted immediately to deliver a new and ambitious bout of debt cancellation for developing countries. By doing so they would play their part in saving many lives.

But instead they appear to prefer the drip-feed approach, giving small amounts of debt relief occasionally and with tough conditions attached. According to economist Jeffrey Sachs, The guiding principle of official debt relief in the past twenty years has been to do the minimum possible to prevent outright disaster, but never enough to solve the debt crisis.<sup>30</sup> In effect, creditors simply demand their money back, occasionally giving more time to pay, while interest continues to accumulate.

Twenty countries have benefited from the HIPC scheme, with a further nine possible beneficiaries in the foreseeable future. Only a handful of other countries have received debt relief on any significant scale. Iraq's 80 per cent cancellation was a result of political pressure from the US, while Nigeria's debt cancellation deal was spurred by the threat of repudiation.

Until now, Christian Aid has never advocated unilateral action by debtor countries, always preferring a multilateral approach to solving crises. In September 2005, Christian Aid published a ground-breaking report calling for a completely new approach to debt crises. *What About Us? Debt and the Countries the G8 Left Behind* demonstrated that today's decisions about debt relief are made by a cartel of creditors who are acting out of self-interest and clear political motivation. Many people in debtor countries believe that creditor countries are deliberately keeping them indebted to maintain power over them.

Christian Aid's report outlines a new and fair system to help countries out of debt crises. Under the present system, when a debtor has to choose between repaying its debts and meeting the basic rights of its citizens, it has to ask for a meeting with its creditors (usually the Paris and London Clubs and the IMF) and request a 'rescheduling'. Under the proposed alternative mechanism, debtor countries could call for the convening of an ad hoc panel with neutral parties, probably based at the United Nations (UN). Many existing arbitration panels could serve as a model for this.

#### **Six key elements of a fair mechanism for dealing with debt crises<sup>31</sup>**

- **Debtor's right to petition:** Sovereign debtors would hold the unconditional right to petition to enter the insolvency procedure.
- **Neutral assessment and impartial decision-making:** Unlike the present system – where the creditor plays the role of plaintiff, judge and jury – the new system would enshrine the proper independence of the insolvency court.
- **Transparency:** Negotiations would be recorded and open to public scrutiny.

- **Participation:** Civil society would have the right to access information and to be heard during negotiations.
- **Sharing the burden among creditors:** The idea is to be fair to creditors as well as debtors. All creditors (including the IMF and the World Bank) should shoulder their fair share of any debt cancellation.
- **Freeze on repayments:** There would be an automatic standstill of debt payments to all creditors during the process.

The panel's aim would be to assess how much of a country's debt could be repaid without jeopardising the basic human rights of its citizens or its ability to reach the millennium development goals.<sup>32</sup>

The independent panel would try to ensure that the debtor emerges from the proceedings with good prospects for financial and economic stability. Because it is sometimes difficult to decide what parts of a country's debt is odious, the panel would also be charged with making impartial decisions. Any odious debt would simply be cancelled.

Once established, a fair, transparent process will have a positive impact on future lending practices. Lenders will know that they can no longer get away with odious lending because odious debt will be written off. Increased civil scrutiny of the process can only lead to better lending and borrowing decisions.

Christian Aid continues to believe that this is the most sensible response to a problem that shows no sign of going away. But more than a year on there has been little response to our proposal from most creditor governments. So now, alongside its partners and colleagues around the world, Christian Aid is articulating the possibility of debt repudiation – the simple refusal to pay.

#### **Definition of terms**

- **Default:** The failure to repay a loan, or interest on a loan, when due.
- **Repudiation:** The refusal to acknowledge a debt. This differs from default as it is the refusal to pay, rather than the inability to do so.
- **Moratorium:** The temporary suspension of payments on a debt.

#### **Costs and benefits of repudiation**

Jeffery Sachs is one of an increasing number of development economists who suggest that, if creditors continue to refuse to budge on debt, 'poor nations should act unilaterally'.<sup>33</sup> Speaking over four years ago, Sachs suggested the money saved from refusing to pay creditors should be registered transparently and used for urgent public healthcare needs.

Christian Aid is not calling on countries to repudiate all their debts tomorrow. Rather we are calling on debtors to take seriously the option of unilateral action, including repudiation of part or all of their foreign debt. We are hoping for two outcomes:

1. Some countries will decide that the balance of costs and benefits of repudiation actually fall on the side of unilateral action and will limit debt repayments in order to pay for vital services with the tacit or public support of sympathetic creditors.
2. Equally importantly, we hope that a serious discussion of repudiation will take place among decision-makers with a positive impact on national and international politics.

Repudiation is not a new idea. Many countries, including today's developed countries, have repudiated debt in the past. The doctrine of 'odious debt' dates back to the end of the 19th century, when the US government repudiated Cuba's external debt after seizing the island in the Spanish-American war. America's authorities argued that Cuba's debt had been incurred without the consent of the Cuban people, and that foreign loans had helped to finance oppression.

The Americans got away with it, but those who reject repudiation point to a number of historical examples of countries that have suffered after choosing to repudiate. Refusing to pay debt can be costly because creditors' penalties for any nation going down this road have traditionally been severe, and the resultant economic squeeze has caused real hardship for poor people.

Repudiation has even triggered invasion, such as when France invaded Mexico in the 1860s after the Mexican president suspended interest payments to foreign countries on loans made by previous governments.<sup>34</sup>

But while there are certainly costs associated with not paying, there are also costs for paying. Or, put another way, there are significant benefits to be had from not paying. These benefits need to be weighed up when countries in debt crisis assess what action to take on behalf of their people.

### **Benefits downplayed**

The moral case for refusing to service debt is strong when people in your country are dying of poverty. The debt cancellation campaign that gathered so much global support in the 1990s, and the Make Poverty History campaign in 2005, both highlighted the scandal of developed countries receiving huge payments that left other nations unable to deliver the most basic services to their people.

Ideally, creditors would show humanity and not require the repayment of loans in such circumstances, but their generosity to date has been very limited.

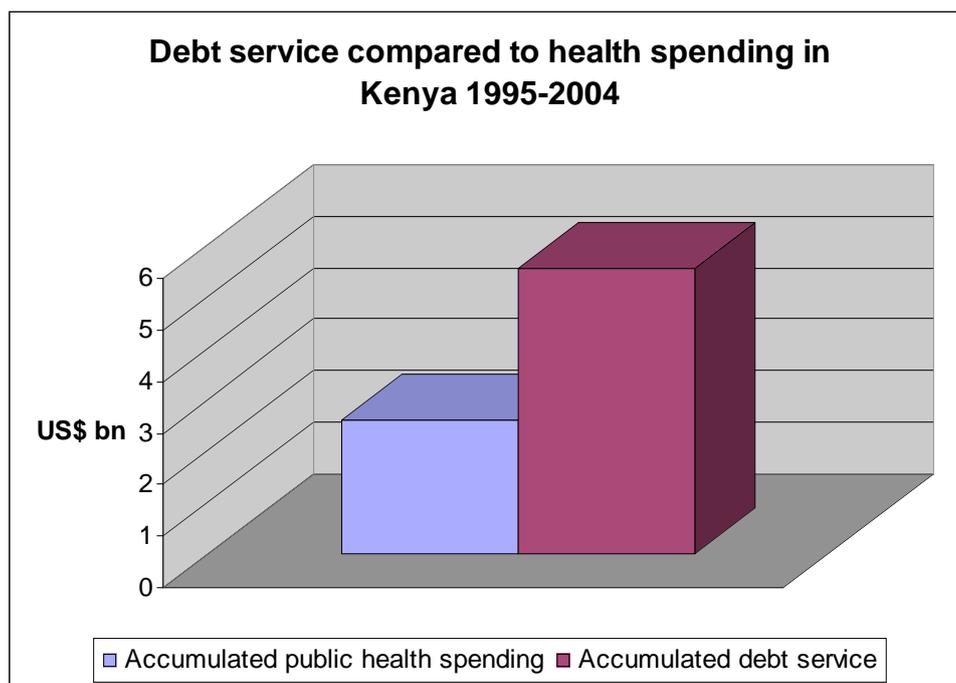
But the case is not just moral. The **simple economic costs of continuing to pay** are often ignored. Servicing public debt means reduced investment in infrastructure, such as roads and ports; in basic and higher education; in healthcare systems and fighting the HIV and AIDS pandemic. It means there is less money available to fight crime, end conflict and support the growth of business, regulatory authorities and other developing institutions. All of these are vital to creating viable states that can achieve sustainable development and reduce poverty in the medium to long term.

## Kenya – what could have been

Kenya is currently facing a major health crisis. Since 1995, average life expectancy has fallen from 53 to 49 years, and female life expectancy from 55 to 47.<sup>35</sup> Infant mortality increased from 62 per thousand in 1993 to 78 per thousand in 2003, and under-five mortality rose from 96 births to 114 per thousand births in the same period. The percentage of Kenya's children who are fully vaccinated dropped from 79 per cent in 1993 to 52 per cent in 2003.

There are many reasons why Kenyans are getting sicker. One major factor is the country's HIV epidemic that has proved inherently difficult to control. In theory, HIV *is* controllable and the overall health crisis *is* preventable. But the reality on the ground is very different. The need for public spending on healthcare, both short-term emergency care and long-term infrastructural development has never been clearer and more urgent.

But the Kenyan government spent almost twice as much on servicing its US\$5bn of external debt between 1995 and 2004 as it did on healthcare. Kenya is not part of the HIPC scheme because it has a good record of repaying debts on time. It is not negotiating for any debt cancellation, despite a growing campaign within the country to do so.



One can only speculate how many lives would have been saved had the Kenyan government been able to spend that US\$5bn on responding to its citizens' desperate healthcare needs.

According to Jane Machira, a Christian Aid staff member working on HIV issues in Kenya, 'The health crisis is ravaging Kenya's economy. Those purporting to be concerned about Kenya's economic growth should worry about the 500 people of working age dying every day of AIDS, many of them teachers and other essential workers, and of the burden placed on struggling families.'<sup>36</sup>

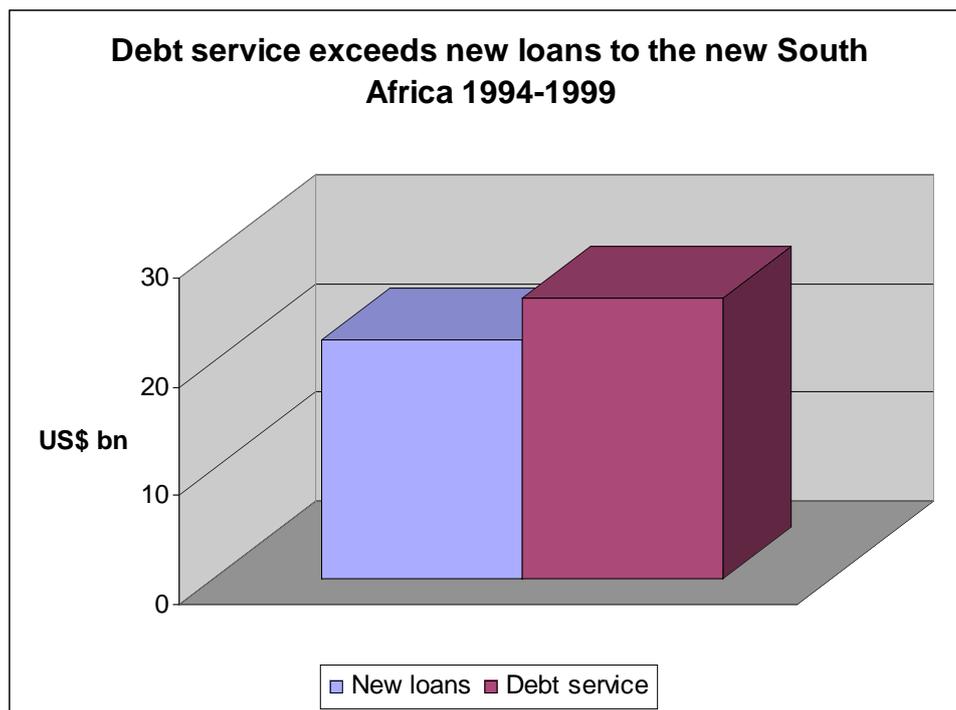
Repudiation may have costs, but the benefits it could bring Kenya are quantifiable – not just in terms of human lives saved, but in terms of an economy with healthy and educated workers concentrating on growth and development, not crisis management.

The benefits of repudiation have not been sufficiently analysed. After a decade or two of toying with alternatives such as private-public partnerships, the consensus has returned to the fact that only substantial public investment can deliver the improvements in living standards and infrastructure that are vital – not just for humanitarian reasons, but for simple economic ones.

### South Africa – the price of payment

During the 1980s, the ANC clearly signalled that they would not honour the debt that had helped to prop up the apartheid regime. But once in power, the party came under immense pressure not to repudiate. Nelson Mandela was warned that he would be **politically ostracised**, while the carrot of new loans – and the corresponding threat of no new loans – was dangled in exchange for paying off the old debt.<sup>37</sup>

However, that carrot was rotten. Between 1994 and 1999, South Africa paid out US\$4bn more in debt service repayments than it received in new loans. The figures for private (non-governmental) debt are even starker. While only US\$4bn of new loans were granted between 1994 and 1999, more than US\$10bn was paid back.



In other words, if South Africa had simply repudiated the odious apartheid debt it would have been US\$4bn better off. Its foreign aid during this period was only just over US\$1bn, so even if aid had been cut off in retaliation by unsympathetic official creditors, South Africa could have profited by US\$3bn.

This example assumes a worst-case scenario regarding international sympathy for South African debt repudiation, which seems unlikely given President Mandela's international acclaim at the time. For a country struggling with rising crime, an HIV

epidemic and the challenge of educating the majority of the population, three billion dollars would have gone a long way.

### **Exaggerated costs**

Debtor countries are traditionally threatened with a range of penalties if they default on loans, and the received wisdom is that they will suffer terribly. The threats are not idle. When Alan García became president of Peru in 1985 at the height of a debt crisis, he announced that he would limit the country's repayments to ten per cent of its export earnings, arguing that 'Peru's biggest creditor is its people'.<sup>38</sup> But when Peru missed a payment deadline to the IMF in July 1986, it was declared ineligible for future loans. The IMF office in Lima was shut down.<sup>39</sup>

García's attempt to stand up to the international financial community is generally considered as a failure. The freeze on IMF lending was copied by many other potential lenders and investors, while penalties and arrears led to a steep build-up of debt. Eventually Peru was forced to give in and pay up. More recently, disbursements from the World Bank to Haiti were suspended between September 2001 and January 2005 as a result of overdue payments.

Pascoal Mocumbi, prime minister of Mozambique from 1994 to 2004, put it well when he said: 'If I stopped paying debt service, all my poverty reduction money would stop from the World Bank and IMF. Fifty per cent of our budget is from donors. I can't not pay – the country would stop.'<sup>40</sup>

Dr Mansur Mukhtar, director general of Nigeria's Debt Management Office also expressed concerns about the consequences of repudiation when parliamentarians discussed it as a serious option. Speaking in March 2005, he said: 'If you do this kind of action, it affects your standing and reputation [in the international community]. It could also affect the kinds of benefits and could have negative impact on the kinds of possibilities that you have to engage in fruitful, economic and financial relationships with other countries. That is the risk.'<sup>41</sup>

However, this worst-case scenario is sometimes exaggerated. While the case of Argentina (see box) is unique because of the huge amount of money Argentina owed to multilateral lenders (US\$32bn, including US\$15bn to the IMF), it demonstrates an important principle – investment doesn't bear grudges, it follows profit.

### **Argentina – a victory by default**

In December 2001, the Argentine government fell amidst mass protests, rising unemployment and the collapse of the peso. This signalled the end of an economic experiment that, until a few years earlier, had been widely regarded as a proud example of free market reform. In the midst of economic turmoil, Argentina defaulted and announced a unilateral moratorium on the repayment of its public external debt.

Argentina's deep economic decline continued following the default. But the default did not cause the decline. It was the other way round – dire economic circumstances left Argentina with little choice but to default on its debt payments.

By 2002, the economy was at rock bottom, with first-quarter GDP down by 16.3 per cent on an annual basis. The banking system had collapsed and bank accounts were frozen.

Official unemployment peaked at 21.5 per cent with another 20 per cent underemployed. More than half the population had sunk below the poverty line.<sup>42</sup>

Throughout this period, Argentina was negotiating with the IMF for a rescue package that would help the economy recover. But the IMF continued to recommend the same harmful policies, such as decreasing the money supply, which had drawn out the economic depression. It also used the opportunity to demand politically unpalatable changes that were unrelated to economic recovery.

On 25 May 2003, Néstor Kirchner was sworn in as president. He pledged not to 'return to paying debt at the cost of hunger and exclusion of Argentines'.<sup>43</sup> He appeared to be prepared to stand up to the IMF by refusing to implement at least the most unreasonable and harmful policies it was pushing for.

Kirchner announced that the government would offer only about 25 cents on the dollar to the private holders of its defaulted debt. After much complaint and lobbying, a large majority of Argentina's creditors surrendered their claims before the deadline of 25 February 2005 in exchange for new bonds worth roughly 35 cents on the dollar.

Argentina had broken the rules in a spectacular way: a huge sovereign debt default, combined with what was widely denounced in the business press as a refusal to bargain with creditors, and a dangerous confrontation with the IMF and its backers. The consensus amongst the experts was that Argentina would suffer severe long-term consequences, such as a long drawn-out depression and isolation from international markets.

But the result has been quite the opposite. The spectacular post-default growth of the economy has surpassed even the rosier predictions. Within a few months of the default, economic recovery was underway in Argentina and there was positive growth in the last three quarters of 2002. The economy grew by 8.8 per cent in 2003 and 9 per cent in 2004 and is still going strong with fundamentals having improved significantly since the successful debt restructuring. Unemployment dropped from 14.5 per cent in 2003 to 12.1 per cent in 2004.<sup>44</sup> Investors have started to return, especially after a bond rescheduling in April 2005.

As *The Economist* put it: 'Capital markets appear to have a remarkably short memory.'<sup>45</sup>

The costs of repudiation vary depending on context and can be exaggerated. For instance, the threat of a cut in the flow of foreign investment is not much of a threat for countries that hardly receive any foreign investment anyway. Equally, very indebted countries often take out new loans to service their outstanding debt. If that debt is repudiated, a shortfall in lending may not be devastating.

Deliberately punishing countries for defaulting or repudiating is a political act intended to reduce the likelihood of any countries choosing to default. Markets themselves tend not to be interested in political statements – if the economic circumstances are agreeable, there will always be investors.

Although investors will look at a country's history of defaulting on debt repayments, it will not be the only factor they consider. If a country decides against servicing its debt obligations in full – not in order to make a cheap buck, but as part of a well thought-out plan to reinvigorate the domestic economy – investors may well see this as a sensible

decision, making the country more attractive as an investment possibility. That is what happened in Argentina. Investors interested in the long term are more likely to be attracted to a country investing in the factors that lead to economic growth, such as a healthy and educated workforce, than one buckling under the weight of never-ending debt payments.

State creditors and multilateral lenders are more likely to make political gestures when faced with default and/or repudiation. But the global political context has changed in the last 20 years. In the 1980s, countries choosing to default found no backing in developed countries. But today, especially in Europe, a large group of people advocate justice for developing countries. These campaigners would put pressure on their governments to be sympathetic with repudiating countries and to avoid launching retaliatory measures.

### **Debtor cartel**

One of the reasons Argentina was able to default was because of its vast outstanding debts. As the saying goes, if you owe the bank £100 you are in trouble, but if you owe the bank £1 million, the bank is in trouble. Nigeria's large debt also placed it in a relatively strong negotiating position. Both countries received only small amounts of aid every year, and a fraction of what they paid in debt servicing. Moreover, the price of oil had recently hit record highs and Nigeria had built up a significant reserve fund before it decided to threaten repudiation.

Smaller countries who threaten repudiation on their own may have a tougher time and are less likely to be able to negotiate decent deals with international creditors. It is with this in mind that campaigners are now considering collective action. Just as creditors club together in the Paris and London Clubs to maximise their negotiating power, the smallest and poorest developing countries might consider acting as a group in negotiations with creditor countries to achieve quicker and fairer outcomes.

On its own, Peru was unable to renegotiate its debt on favourable terms. But had it joined forces with other Latin American countries, the resulting cartel may have been powerful enough to win negotiations with creditors.

### **Shifting the terms of debate**

While repudiation may be both morally and economically defensible for some countries, it is unlikely in the short term that many countries will adopt this bold approach. But it is not only the final act of repudiation that could be beneficial for poor countries. Simply debating the issue can bring about important side effects.

The existing debate about debt relief and cancellation is very narrow in scope. Creditors tend to define what is considered 'possible' in ways that suit them. One of today's cheerleaders of debt relief – the UK Treasury – considered the very idea of substantial debt relief to be an economic impossibility in the early 1990s.

That all changed with the onset of HIPC, which resulted not from a change in economic realities, but from large-scale public pressure to do something. Even then, multilateral lenders were considered to be beyond the remit of serious debt relief – debts to the World Bank and IMF were to be paid back at all costs. But in 2005, that frontier was rolled back too, again as a result of political pressure from people all over the world campaigning for justice.

As the limits of the HIPC initiative grow more apparent, we need to constantly re-examine what is 'possible'.

Domestic politics would change in countries where a practical, focused demand for repudiation is popularised. Systems of accountability would come under renewed scrutiny. The cycle of borrowing and accepting external conditions would no longer be business as usual. People might start to realise that their governments need not be ineffectual players in international politics, but in fact have some real power and real options.

We are calling for a debate on debt repudiation, because we believe such a debate is natural and sensible when a society begins to demand that its leaders take a bold stand for genuine responsibility and accountability. By arguing that repudiation should be considered, we are moving away from asking for favours from the most powerful actors in the global economy.

The political discourse can be shifted. If debt is not generally discussed in a country', a debate about the possibility of repudiation can force it onto the agenda. If calls for debt cancellation are already routine people might start considering more proactive measures.

The process of debating repudiation could bring about many positive changes. These range from educating the public in indebted countries about the illegitimacy of their debt and the fact that their governments can refuse to pay it; to winning concessions from creditors when they realise that a country's people are not going to stay on the debt treadmill indefinitely.

#### *Government accountability*

Demands for repudiation must emanate primarily from within the debtor country itself. Many campaigners in developing countries have begun national debt audits. As well as helping to demonstrate why repudiation is a reasonable option, these audits will support the process of holding governments accountable for their borrowing decisions by:

- exposing political systems for borrowing and spending money, subsequently making them the subject of focused campaigning
- focusing politicians and the public on examining loans *before* the contracts have been signed
- bolstering legal investigations and actions designed to increase governmental accountability

#### *Concessions along the way*

When the Nigerian legislature threatened repudiation, the Paris Club reversed its refusal to negotiate bilateral debts. The resulting agreement was controversial because Nigeria ended up paying a vast amount of money up-front in return for significant debt cancellation, but there were other options that could have been more clearly positive. Simply talking the language of repudiation can sometimes increase a debtor's negotiating power in subsequent talks. For example, a temporary suspension of debt payments – a moratorium – might be more politically feasible in certain contexts than full repudiation. In many contexts repudiation of part, rather than all of the debt, is a

plausible option. There are many other possibilities for reducing the money allocated to debt.

## **Nigeria**

A fifth of all Africans are Nigerian, and most Nigerians live in absolute poverty. The most recent statistics available (from 1996) suggest that 91 per cent of its population – 124 million people – live on less than US\$2 per day.<sup>46</sup> Nigeria was removed from the list of countries that would receive debt relief under the HIPC process, probably because canceling its debts would be too expensive. It was only after Nigeria made a genuine threat of repudiation that its creditors finally came up with a deal – albeit not a very generous one.

In 2003, Nigeria paid US\$1.6bn in debt repayments, more than its combined spending on healthcare and education. It owed more than US\$34bn to foreign creditors, most of which was built up under military dictatorships supported by institutions and companies from developed countries.

Since 1999, a new administration under President Olusegun Obasanjo has committed Nigeria to a path of reform and democracy. But despite numerous meetings with creditors, President Obasanjo's appeals for urgent debt cancellation fell, until recently, on deaf ears.

Demands were increasing for more spending on social infrastructure – including education, healthcare and roads – and the need to fund the judiciary and an expanding police force. The House of Representatives, Nigeria's lower legislative chamber, therefore passed a motion in March 2005 asking the executive to unilaterally stop repayments on debt. The motion highlighted the fact that creditors' interest and penalties had turned Nigeria's debt into an unbearable burden: '[Nigeria's] debt stock as at 1985 was about \$19bn and between the said 1985 and 2005 Nigeria has repaid a total of \$37bn to all its creditors including the Paris and London Clubs of creditors (...) [Despite this] the debt stock as at December 2004 was \$35bn outstanding to all external creditors of Nigeria.'

The motion was however not passed by the senate, the upper legislative house, which agreed with President Obasanjo that it was appropriate to give creditors one more chance to negotiate a settlement before opting for the extreme route of repudiating debt.

In his response to the vote by the House of Representatives, President Obasanjo spoke of his frustration at creditor countries' refusal to move on the issue of debt cancellation for Nigeria. He said: 'I have done everything I can in the last six years, travelled extensively, got promises, but any time we are nearly there, they would give another condition.' He added that if his appeals 'fall absolutely on deaf ears, then I will come back and report to you, House of Representatives'. This was a veiled reference to a threat of unilateral action.

In June 2005, a deal on Nigerian debt finally emerged from the Paris Club. Although it is too limited in scope, failing to reflect properly the debt's odious nature or the desperate situation of many poor Nigerians, at least it marks an end to the huge debt that was strangling the Nigerian economy.

Creditor countries put the deal down to the Nigerian government's implementation of economic reform programmes. However, as recently as April 2005 the media reported that Paris Club members were privately scornful about the possibility of doing any deal with Nigeria.<sup>47</sup>

In fact, what had really changed was that the Paris Club had realised that Nigerian parliamentarians were serious about their threat to repudiate. Without the threat of repudiation, Nigeria would probably at most have been offered yet another lame round of debt restructuring but not for another few years.

## Conclusion and recommendations

We have established that unilaterally withholding debt repayments brings both costs and benefits. In the past, the costs have been emphasised and the benefits left largely unacknowledged. Today, any country with serious debt problems should look at this equation again. The result of their analysis will differ from country to country. Some may choose to avoid the politically difficult route of repudiation and seek to reduce their debt burdens in other ways. For example, the HIPC scheme holds possible benefits for the nine 'decision point' highly indebted poor countries.

But others have few options open to them. Rescheduling and small-scale debt swaps are unlikely to eradicate the burden of debt. In these cases, countries may decide that the benefits of repudiating their debts outweigh the costs. Others may see total repudiation as a step too far, and may wish to set an upper limit to the percentage of government expenditure that should be allocated to debt repayments.

Debt repudiation on its own will not make much difference unless it is accompanied by reforms that will benefit poor people and efforts to boost the economy. Christian Aid is calling on developing country governments to implement policies promoting poor and excluded people's welfare. Whatever route these governments choose to take, they should be supported if they are trying to respond constructively to their citizens' desperate need.

### **Christian Aid recommends that when assessing what action to take with regard to their debt problems, debtor countries should:**

- reassess the impact that debt servicing is having on their economic prospects
- carry out a full debt audit to assess how much of the debt is odious or illegitimate and should therefore not be repaid
- assess the portion of their *remaining* public debt that can be serviced without jeopardising the delivery of basic services (such as basic healthcare and education) to the country's citizens. This may be all of the remaining debt in some cases
- call a moratorium on servicing illegitimate debt and payments that are jeopardising basic welfare. Discuss next steps with creditors
- depending on the progress of discussions, look at the possibility of withholding payment in part or in full, with the intention of transferring the money to invest in basic services and vital infrastructure. Carry out a cost-benefit analysis of this course of action. Act accordingly
- work with allies to develop like-minded country groups in order to negotiate better with creditors
- open debt contraction processes to full democratic scrutiny.

**Christian Aid recommends that creditor countries, international financial institutions and private sector creditors should:**

- support countries that choose to place their people's welfare and economic growth above creditors' requirements. This may involve financial cost to the creditors
- develop a fair and transparent arbitration process to resolve debt disputes and debt crises that leave countries unable to fulfil their citizens' basic human rights.
- accept responsibility for playing a part in debt build-up, especially in the case of illegitimate debt.

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