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External Debt Management for African Countries

Katsuya Mochizuki

Africa's current financial crisis is a tragic legacy of the debt management strategy of the 1980s. Africa became more debt distressed than any other region in the world. The U.N. Secretary General once remarked that this external debt is a "millstone" around the neck of Africa. Africa's overall economic situation deteriorated as the debt burden worsened in many of the region's countries, and some are even seen to be in a "debt trap" or a "debt treadmill," which forces them to obtain new financial resources simply to repay old debts.

Contribution of Financial Flows

The rapid recovery of financial flows to developing countries has been remarkable. The World Bank's *World Debt Tables* attests to this phenomenon. The volume of private capital flows has been increasing since the late 1980s. In 1993, it jumped by more than 50 percent over the 1992 level. However, private flows, especially portfolio stock investments, are not necessarily favorable for developing countries because of their unstable nature. The present flows should, therefore, be regarded as a temporary phenomenon.

As for foreign direct investment (FDI) flows, the share going to developing countries has been increasing since 1990. By 1993, it reached 37 percent of total FDI flows, up from 29 percent in the previous year. FDI is important for developing countries because of its debt-free nature. Nonetheless, FDI, too, has its drawbacks. Its direction or trend is rather biased and the poorer countries often have few chances of enjoying its benefits.

On another front, official flows have been flat since the late 1980s. Compared to private flows and FDI, aid flows on the whole show less fluctuation as the amount of grant aid to poorer countries generally has grown steadily, but comparatively more slowly than private flows. Hence, despite the recent increase of official development aid, the debt structure of African countries remains substantially unchanged.

Essence of the African Debt Problem

Although all types of financial flows have increased, African economies are still in a critical situation. For many, expenditures continue to exceed earnings. Most of the African economies are under structural adjustment regimes, implementing programs and measures to reduce government expenditures. They endeavor to improve their balance of payment and fiscal discipline. Despite their efforts, one more aspect of this problem is beyond their reach.

The root of their problem is their heavy debt burden. On the bright side, the commercial debt problem appears to be coming to an end—even among the African economies. Negotiations with the London Club have gone smoothly, and commercial bank debts outstanding could be settled when Brady-type operations are initiated. The restoration of private flows is a sign of confidence from foreign creditors, but official debt management is still under way.

African countries are still suffering from high debt stocks. As mentioned above, the economic crisis deepened as the debt stock deteriorated for African countries. With the failure of a series of debt initiatives, official debt burdens were not relieved. As a result, multilateral debt payments became far heavier in sub-Saharan Africa's debt profiles. In spite of its comparatively small share, multilateral debts are a far heavier burden than bilateral debts for African countries.

Of the total debt stock of the severely indebted low-income countries (SILICs), the share of multilateral debt was 25 percent in 1993. In addition, another 4 percent is owed to the International Monetary Fund (IMF). Since nonconcessional multilateral debt (including that owed to the IMF) accounts for less than 6 percent of the total, it is obvious that the IMF debt is far from a small burden for these countries.

Measures to Be Taken by Multilateral Institutions

The most likely source of initiatives to deal with this debt problem is the IMF itself as it is the gateway to fresh financial flows. Relentless and uncompromising enforcement is one way to check loose policies and growing debts. As the economic conditions in African countries continue to deteriorate, some immediate measures must be taken.

A common complaint among debtor countries is that repayment to the IMF takes precedence over all other debt service requirements.

Since IMF decisions are critical to these countries' access to funds, their commitment to IMF policies is a priority in their debt management. Unfortunately, the IMF has not taken any major steps to lead these countries out of their predicament. There is an apparent lack of coordination mechanisms within the creditor community to deal with this overall debt crisis. The Paris Club is important in providing a framework of debt relief, but its operational structure lacks clarity.

In the official aid community, the Consultative Group (CG) and the Aid Group have performed effectively as coordination mechanisms. They have a definite base of establishment and have shown concrete results. Another merit of these mechanisms is their ability to work with recipient countries individually with full consideration of their overall economic situation, as well as their distinctive characteristics and needs. Because debt difficulties differ from country to country, debtor countries should not be categorized as a group. From this point of view, the "consortium" mechanism should be extended to other debtor countries.

For those heavily indebted African countries, debt stock reduction is a priority. Certain debt relief measures or debt forgiveness are inevitable. The so-called "Naples terms" are applicable but inadequate. An "exit strategy," mentioned in the *World Debt Tables* for these debtors, should be the goal. "The combination of a reduced debt overhang, sound domestic policies, and new financial flows on a concessional basis should help reduce the uncertainty about the economic prospects...." And multilateral institutions are expected to take the lead.

Finally, a word on the role of bilateral official creditors. These countries are leading the debt management debate through the Paris Club and other international fora. By setting forth a series of initiatives, they have created an indispensable role for themselves. Nonetheless, the spread of "aid fatigue" has compromised their real and perceived contribution. The idea of effectiveness, therefore, should also be introduced in the discussion on debt management.

Multilateral institutions are forerunners in this field. They have successfully mobilized their limited financial resources to implement various measures. Their expertise has allowed them to channel resources from donors to recipients effectively and in a timely manner. In the field of debt management, for example, the Debt Reduction Facility of the International Development Association (IDA) has been shown to be the most effective one for the poorest debtors. This kind of effort needs to be supported by bilateral creditors. Capital replenishment or additional contributions to multilateral institutions should be considered in line with those measures.