

The Paradox Of Foreign Debt To Third World Nations In International Politics: A Rationale For Perpetual Dependency

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Abstract :

The paper examines some of the fundamental issues of dependency and underdevelopment in our contemporary international economic and political relations. The paper also analyses the paradox of foreign debt, which is supposed to be debt for development and financing development projects, but used as an instrument to perpetuate third world domination through financial imperialism. By adopting the secondary methodology, the paper discovers that, both advanced societies of the world and leaders of the third world are developing underdevelopment in the third world. The paper concludes that, third world indebtedness only exacerbates third world dependency on the economies of the advanced industrialized societies in this twenty first century. The paper recommends humanitarian aid to the third world against strategic aid, among other things.

Key words: *paradox; foreign; debt; crisis; international politics; economics.*

Introduction

The issue of debt is one that is inherent in international economics and politics. Albeit no nation want to be a debtor, but some internal or domestic forces compel nations to be indebted, especially to the international monetary fund. Some of these debts are sometimes used for developmental purposes and sometimes for selfish interests of politicians who in turn siphon the money borrowed with the name of development plans.

As noted above that borrowing comes in a situation where by a nation has some developmental projects to finance and the

resources are limited, that nation can go ahead to borrow some money for financing such capital projects, but not without implications. As in the view of Audu (2013):

Foreign borrowing, even though can be beneficial, providing the resources required to promoting economic growth and development, it has its costs. In recent years, these costs have greatly outweighed the benefits for many Third World countries. The main cost associated with the accumulation of large external debts is debt service- that is, the payment of

amortization (liquidation of the principal) and accumulated interest.

Debt can be classified into reproductive or dead weight debts (Audu, 2013). Debts are reproductive when they are meant to serve as instruments for developmental projects. They are dead when their purpose is to serve wars and projects that are not to yield any sort of developmental aspect.

The dynamics of foreign or internal debt according to Audu (2013):

Depends on whether it is external or internal debt. When a country obtains a loan from abroad (bilateral or multilateral) it means that the country can import from abroad goods and services to the value of the loan without, at time having to export anything to exchange when the capital and interest have to be repaid, the same country will have to get their burden of exporting goods and services without receiving any imports or exchange for debt financial investments need to be productive and well managed enough to earn a rate of return than the cost of debt service.

Material and method

The material used in this research work was obtained from documented literatures under library research, which in the parlance known as secondary methodology. The material and method

is also aided by a theoretical instrument, which provides more scientific backing to the arguments raised in the paper. The theory adopted therefore, is the dependency theory, which provides a critical explanation of why the third world is dependent on the economies of the euro zone and America, and of which the dependency theorists see foreign aid as a contributing factor.

In a definition given by Osvaldo (1969), Dependency can be defined as an explanation of the economic development of a state in terms of the external influences such as political, economic, and socio-cultural, on national development policies. The above definition provides rather, an influential approach to the study of dependency, focusing on political factor, economic or cultural forces that shape the internal conditions of economies of the dependent nations. But just as Marxists analogy of historical and dialectic materialism, Theotonio Dos Santos emphasizes the historical dimension of the dependency relationships in his definition:

Dependency is...an historical condition which shapes a certain structure of the world economy such that it favors some countries to the detriment of others and limits the development possibilities of the subordinate economics...a situation in which the economy of a certain group of countries is conditioned by the development and expansion of

another economy, to which their own is subjected (Theotonio, 1971: 226).

It is therefore notable from the above definition that, foreign debt is another medium through which the advanced capitalist economies have conditioned the economies of the third world to an extent they (the advanced nations) make the whole process favors them. This is done for the expansion of European economies (Amin, 1976; Bornschier, 1976; Cardoso And Falsetto, 1979; James, 1997).

Foreign Debt and Third World Debt crisis

Debt crisis has assumed a prominent dimension in the third World countries as is making development very difficult. Third World countries are so tied to debt trap to the extent that virtually all their foreign exchange earnings are spent on debt service.

In the period between 1970 and 1992, the external debt of developing countries grew from \$68.4 billion to just under \$2trillion, an increase of more than 2,000%. The debt crisis has truly become a worldwide problem with serious economic implications for both developed countries and Third World Countries. In fact, the debt crises of the 1980s called into questions the stability and viability of the international financial systems.

The external debt crisis of sub-Saharan Africa like its Latin American and other Third World Countries is not yet over. A significant number of

countries in the TWCs adopted a development strategy that relies heavily on foreign financing for both official and private sources. This according to Ajayi (2003:105) has meant that:

For many countries in the region the stock of external debt has built up over recent decades to a level that is widely viewed as unsustainable. This has given rise to concerns about its deleterious effects on investment, development and principally the well known debt overhang. In Nigeria for instance, external debt is 65% of Gross Domestic Product (GDP) while annual debt service is nine times the annual health budget. Domestic debt is also an issue, ballooning to an estimated US \$8.6 billion by the end of 2001.

Foreign debt has further compounded the development crisis of the TWCs. According to Ghali (1992), talking about Africa and debt crisis, he described the external debt as a millstone around the neck of Africa. The debt burden creates difficult problems for the economic recovery programmes of most TWCs. For many African countries, multilateral debt servicing is currently both large and burdensome part of their obligation. As part of the effect of foreign debt on TW economies, it discourages investors. Foreign investors will not risk funds if domestic investors are not prepared to take the same risk. In Africa

for instance, until 1970, debt was not an issue in the development of African countries. The reasons for this development can be attributed to the followings:

- i. The early post independent period in Africa did not witness any significant growth in the level of opportunities for the expansion of foreign investment capital.
- ii. Most African states found it difficult to raise loans from the international capital market as private banks were wary about advancing loans to Third World countries in the 1960s.
- iii. The ideology of development that predominated the 1960s acted to discourage heavy borrowing by Third World countries from the international capital markets and this was thought to be inappropriate for normal economic wisdom.

However, in the 1970s, the situation changed and most western creditors became anxious to offer loans to African countries. The reasons for this state of affairs according to Bangura cited in Ujo, (1995:143) include:

The world capitalist crisis which started in the early 1970s created a serious problem of profitability for many multinational companies. A serious problem of realization was also created in which firms found it difficult to sell their products. Because of the general drop in business, banks were unable to make new borrowing as

investors were skeptical about the investment climate and the prospect for global economic recovery. The events surrounding the Arab-Israeli war of 1973 which led to the Arab oil boycott of the West did not help matters. This is because the quadrupling of oil prices which resulted from the boycott plunged western industrial establishment into a further problem of increased production costs which in turn worsened the realization problem.

A common outcome of the foreign debt crisis throughout the Third World was the increase in the power and influence of IFIs, particularly the IMF and WB, which had greatly diminished in the 1990s. As private sector lending dried up following the Mexican crisis of 1982, the IMF turned from its traditional role of lender of last resort to the only available source of external financial assistance and became the leading agency in the management of the crisis. Consequently, the IMF assumed a key role of restructuring the countries' foreign debt, conditioning financial assistance to the promotion of structural reforms along free market principles. Similarly, WB changed its role from lending money for Third World development projects in areas such as physical infrastructure to the promotion of structural reforms that involved fundamental changes in economic policy.

Consequently, these role changes, the IMF and WB's relations with Third World countries became highly politicized and open to the charge

that unaccountable multilateral institutions were forcing democratically elected governments to adopt policies that hurt the poor and privileged the interests of the foreign interests over the welfare of the people. Foreign debt crisis has increased the IMF's position and influence over the economic and policies of the Third World countries. In addition, conditionality was at its strongest on issues of debt service in the early 1980s, and shifted towards structural reform in the later years and present decades.

Causes of Debt Crisis

In the argument of Shah (2007), debt crisis in the third world impedes political and economic development, and has also paved a way for social and security crises. In his words, he argues:

Third world debt has long been recognized as a major obstacle to human development. Many other problems have arisen because of the enormous debt that third world countries owe to rich countries. Debt has impeded sustainable human development, security and political or economic stability. How has this happened?

Some of the major causes of third world's debt crisis are:

- i. **Continuing Legacy of Colonialism:** In the analysis of South Centre (2004), the history of third world debt is the history of a massive siphoning-off by international finance of the resources of the most deprived peoples. This process is designed to perpetuate itself thanks to a diabolical mechanism whereby debt replicates itself on an ever greater scale, a cycle that can be broken only by canceling the debt. According to a new Working Paper on "Effects of debt on human rights" prepared by Mr. El Hadji Guissé for current UN Sub Commission on Human Rights (E/CN.4/Sub.2/2004/27), the developing countries' debt is partly the result of the unjust transfer to them of the debts of the colonizing States!

- ii. **Odious Debt:** According to Steve (2006), odious debt is an established

legal principle. Legally, odious debt is debt that resulted from loans to an illegitimate or dictatorial government that used the money to oppress the people or for personal purposes. Moreover, in cases where borrowed money was used in ways contrary to the people's interest, with the knowledge of the creditors, the creditors may be said to have committed a hostile act against the people. They cannot legitimately expect repayment of such debts.

This report estimates "apartheid-caused debt" at £28 billion (about \$46 billion at the time the report was written). That is the £11 billion [\$18 billion] that South Africa borrowed to maintain apartheid, and the £17 billion (\$28 billion) that the neighboring states borrowed because of apartheid destabilization and aggression. This is 74% of the present regional debt of £38 billion (\$62.5 billion).

In a comparative study of the third world, Steve (2006) has given the analysis of odious debt of Indonesia, Argentina and Nicaragua as follows:

- a. Indonesia, where in the region of US\$151 billion relating to odious debts has already been 'overpaid'—twice the level of

recorded debt. This means that Indonesia has made a cumulative net transfer to the North of US\$138 billion to date—or 90 per cent of Indonesia's GDP.

- b. Argentina, where in the region of US\$77 billion relating to odious debts has already been 'overpaid'—75 per cent of the country's recorded debt.
 - c. Nicaragua, where the odious debt is over five times the country's total GDP.
- iii. **Mismanaged Lending:** this deals with mismanaged spending and lending by the West in the 1960s and 70s.
- a. 1960s saw the US spend more than it had, resulting in the printing of more dollars.
 - b. Oil-producing countries, pegged to the dollar were affected as the value of the dollar decreased.
 - c. In 1973, the oil-producing countries hiked their prices as a result, earning a lot of money, which they put in to western banks.
 - d. Interest rates started to plummet resulting in more lending by banks to try and prevent a crisis.
 - e. A lot of the borrowed money went to western-backed dictators, resulting in little benefit for most people.
 - f. In 1982 Mexico defaulted on its debt payment, threatening the international credit system.

- g. The IMF and World Bank stepped in to Mexico and other nations facing similar problems, prescribing their loans and structural adjustment policies to ensure debt repayment.
- h. The poor have suffered the most as a result of the harsh conditions of structural adjustment.

Most loans to the third world have to be paid back in hard currencies (which do not usually change too much in value, e.g. the Japanese Yen, the American Dollar, pound sterling and the euro, as identified under the drawing rights of the IMF) with the following assumptions:

- a. Poor countries have soft currencies (values which can fluctuate).
- b. Debt crises can also occur just by the value of the developing country's money going down, which can be due to a variety of other inter-related factors.
- c. Paying off loans implies earning foreign exchange in hard currencies.
- d. Combined with falling export prices for many poor countries, debts become even harder to pay off.
- e. Refinancing loans implies taking on new debts to service the old ones.
- f. Structural adjustment advice in the past from the IMF and others, has led to the cut back on important spending such as health, education, in order to help repay loans.

This has implied a downward spiral and further poverty.

- iv. **The World's Poor Are Subsidizing The Rich:** Another cause for large scale debt has been the corruption and embezzlement of money by the elite in developing countries (who were often placed in power by the powerful countries themselves). These moneys are often placed in foreign banks (and used to loan back to the developing countries). Many loans also come with conditions that include preferential exports etc. In effect then, more money comes out of the developing countries than is given in. This depresses wages even further due to the spiraling circle downwards to ensure that enough exports are produced.

This, according to Smith (1994: 139-141), the world's poor are subsidizing the rich. The net gain to the over-capitalized countries (loss to the under-capitalized ones) of \$418 billion between 1982 and 1990 is more than double what was spent to rebuild Europe after World War II. "Capital flight from Mexico between 1979 and 1983 alone was \$90 billion, an amount greater than the entire Mexican debt at that time."

- v. **Backbone to globalization:** The economic decisions and influence in various international agreements, treaties and institutions by the wealthy

and powerful nations also help form the backbone of today's globalization. That such immense wealth and prosperity for some have come at a time when most nations in the world have steeped into further poverty and debt is no coincidence. The policies of those who have the power and influence have been successful to help raise standards for some in their own nations, but at a terrible cost. Rich nations as well as poor incur debts, but often the wealthier and more powerful ones are able to use various means to avoid getting into the dilemmas and problems the poor nations get into. In fact, the following summarizes it quite well using the U.S. as an example:

The US According to Le Monde Diplomatique, (2000) began by abandoning the system of fixed exchange rates established by the Bretton Woods Agreements in 1944 and introducing a system of generalized floating exchange rates. There was a strong economic motive for the decision, which the US authorities took unilaterally in 1973. They were seeking to compensate for declining competitiveness and a growing national debt by exporting the country's macroeconomic imbalances. The floating exchange rate system provided a flexible and efficient monetary tool that enabled them to avoid the adjustments that would otherwise have been required by America's

new situation as a debtor. In a system of fixed exchange rates and gold convertibility, the US would have been obliged, like every third-world country today, to pay for its indebtedness with a relative loss of sovereignty and highly unpopular domestic austerity measures.

The new system also allowed the US to maintain a high standard of living at home by dipping into the planet's savings. Thanks to its political power and to the dollar, which was the world's only reserve currency, the US was able to keep its monetary sovereignty intact.

Its allies could not question American policy without destabilizing the institutional fabric and the cold-war security system from which they derived undoubted benefits. The burgeoning US deficit was funded for decades by Japan and Europe (*Le Monde Diplomatique*, 2000).

Conclusion

It is pertinent to note that, the aftermath of aid to the European nations after the Second World War was economic and infrastructure reconstruction, which was made possible and available by the United States in its interventionist gesture to salvage Europe using the Marshall plan. It should also be noted that, if Africa and other third world nations could have such humanitarian gesture with the name of Marshall Plan, the economies of Africa would develop into a more favorable condition. But the issue of foreign aid based on strategic gesture, is rather exacerbating the level

of dependency and underdevelopment of Africa, due to the e

xpectations of the donor nations to satisfy their strategic desires.

Recommendation

In order for Africa and other aid receiving nations to move forward, any issue of foreign debt must concur with the following recommendations:

The availability of debt must be based on humanitarian gesture irrespective of the situation in the recipient nation.

Two, the debt given must also be monitored and evaluated to ensure efficiency and productivity.

Three, corrupt leaders who siphon money received as debt meant for developmental projects must be prosecuted to international criminal court to bring back what they have stolen, and serve a special term incarcerated.

The donor institutions must also supervise with sincerity, the projects to be executed in the recipient nations.

Five, foreign debt must also be dedicated and consolidated to and on education, science and technology, infrastructure and security of lives and property.

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