Problems of Foreign Indebtedness of Developing Countries (*)

1. Introduction

The attention of capital-exporting countries has been drawn in recent times to the difficulties of less-developed countries in meeting their heavy and growing foreign commitments on debt service account. A quantitative analysis has been provided by members of the World Bank staff in a series of studies concerning debt-servicing problems of low-income countries (1). In the studies of the Bank particular interest attaches to the analysis of the clear tendency of the service burden to increase on a large number of developing countries. The warning sounded by the Bank against the dangers which might derive from a further increase of such a burden deserves the most earnest consideration.

The first aspect of the problem is how to determine the limits within which foreign indebtedness should be contained in developing countries. The second aspect is how to ensure that, if such limits are respected, the service of the foreign debt will not, in spite of all, impose intolerable strains on the balance of payments of the capital-importing country.

The conclusions of this paper can be summarized in the following terms:

(a) Normally, it would not be correct to expect a developing country to reduce her foreign indebtedness in the early stages of her growth. What we can expect is only a regular payment of interest

(*) The views presented in this article are the author's own and do not purport to reflect the standpoint of the Commission of the European Economic Community.

(1) D. Avramovic and R. Gulhati, "Debt Servicing Capacity and Post-War growth in International Indebtedness", Baltimore, 1958, brought up-to-date with the volume "Debt Servicing Problems of Low-Income Countries, 1956-58", Baltimore, 1960.

and dividends, but no net amortization of the outstanding debt. The level of " sustainable indebtedness " should therefore be determined with reference to the dividend and interest payments which the " goods and services " account of the country's balance of payments can bear in the long run. We should, on the other hand, proceed on the assumption that old debts will be replaced, as they mature, by the inflow of fresh foreign capital.

(b) If only an amount of foreign capital smaller than is economically justified by the economic prospects of the country can be serviced at market conditions, then capital exporting countries should be ready to ease such conditions. Public sources of capital should play an equilibrating role in this respect, so as to keep the service burden within tolerable limits.

(c) No one country can, however, be expected to play consistently such a role of " residual lender " and supply funds at favourable conditions while other countries' capital exports are being serviced at market rates. Therefore the debt-servicing capacity of developing countries should be studied in common by capital-exporting countries and appropriate conclusions should be drawn for the participation of each of them to the development assistance effort.

The following two paragraphs of this paper will sketch the economic background of the problem of estimating the limits to foreign indebtedness. The remainder of the paper will instead be devoted to policy aspects and more particularly to the setting of interest rate, amortization, and other conditions in individual lending operations in favour of developing countries.

2. Foreign indebtedness and the balance of payments

Insufficiency of purchasing power abroad is often among the basic factors limiting the rate of economic growth of a country. Schematically, we can take as a hypothesis that to any given rate of growth of national product corresponds a given rate of increase of foreign exchange needs, which is linked to the former by the normally positive elasticity of import needs in terms of national product. As, on the other hand, the development of foreign exchange earnings is mainly a function of variables external to the country being considered, we may expect that — starting from an equilibrium situation — an increase in the rate of growth of national product will result " ceteris paribus " in a gap in foreign exchange resources. The availability of means apt to fill such a gap becomes then the condition for maintaining the higher rate of economic growth.

What has just been presented is, of course, a rather extreme view of the problem: in the long run, the means to support a higher rate of growth of national product must come from increased savings and exports as well as from import substitution. It is nevertheless true that in periods of growth acceleration, a net inflow of resources from abroad may be the crucial factor for sustained development; particular interest attaches therefore to the study of the evolution over time of such an inflow.

Let us first suppose that foreign capital is flowing in at an increasing rate. This will not be sufficient to avoid balance of payments worries, except under certain specific conditions. It has been shown (2) that annual payments on account of interest and amortization must, from a given moment on, result in a net burden for the balance of payments by overtaking even an ever growing inflow of new capital from abroad, *unless such an inflow grows at a rate greater than the average interest rate which is being paid on outstanding indebtedness.*

On the same lines we may consider a case in which the gross capital inflow from abroad is constant: in this case the *net* inflow will gradually decrease and, from a given moment on, will turn into a net outflow, as the growing burden of service on outstanding indebtedness approaches the gross inflow of foreign capital. However, as soon as annual amortization payments equal the gross capital inflow, indebtedness evidently stops growing and from that point on the net outflow equals the interest payments on a stable foreign debt.

Finally, if the gross inflow of capital were to take place at a decreasing annual rate, the reversal of the net flow would occur earlier than in the previous case and the net negative effect on the balance of payments would at first grow and then decrease gradually, as the outstanding indebtedness is reduced by the effect of net repayment.

From a practical point of view, the two hypotheses that deserve to be examined in greater detail are: (a) that the net flow may

(2) By E. D. Domar, " The Effect of Foreign Investment on the Balance of Payments ", *American Economic Review*, Dec. 1950.

remain positive, and, (b) that it may stabilize at a constant negative annual rate.

As far as the first hypothesis is concerned, the possibility of avoiding the reversal in the net flow of capital appears rather remote. The average " rate of interest " on the outstanding indebtedness will normally be higher than the rate of growth of national product and of exports from the debtor country. As the gross inflow of capital should grow at a rate at least equal to this average " rate of interest " if the reversal of the flow is to be avoided, one should be ready to see outstanding indebtedness and the debt-servicing burden grow more rapidly than production and export earnings. This implies that the country should be prepared to face a liquidity position which is steadily deteriorating.

The second hypothesis, that of a constant gross inflow of foreign capital, is of greater interest because it allows one to look into the concept of " sustainable indebtedness " which is often used in the analysis of development finance. One may remember that, from a given point on, the net burden will consist here only of interest payments on a constant foreign indebtedness (3). Such a level of indebtedness can be considered " sustainable " if the foreseeable development of the goods and services account of the balance of payments will yield in the long run a surplus sufficient to cover its interest burden.

3. Limits to foreign indebtedness

Let us now take a closer look at the concept of sustainable indebtedness. It has been said that the net outflow which must be taken into account consists exclusively of interest payments because, in the hypothesis being discussed, amortization payments are exactly compensated by the annual gross capital inflow. On the plan of the most orthodox economic logic it would not be correct to analyse the ability of a country to sustain a given level of indebtedness by looking at its ability to obtain in the " goods and services " account a surplus sufficiently large to cover payments of *both* interest *and*

(3) If we call K the average amortization period of loans received from abroad, it can be shown that the debt will stabilize after $K+1$ years and will at that time amount to the gross constant annual inflow multiplied by $\frac{K+1}{2}$.

amortization, as if the whole of the foreign indebtedness were to be liquidated in a period corresponding to the repayment schedule of a typical loan. In reality, " while individual loans are repaid, other loans are obtained to replace them, so that the whole of foreign debt can be considered as a revolving loan. What matters is that, once the level of sustainable foreign indebtedness has been reached, no further net indebtedness takes place, even if on a gross basis the country will have to go on obtaining new loans from abroad. On such a basis only an interest burden — which might be of the order of 5-5½ — should be considered in the appraisal of the country's solvency, while amortization payments should not be included " (4).

What has just been said is perfectly consistent at the level of pure theory: a *net* repayment of foreign debt should not take place until the difference in yields which originally stimulated the international movement of capital has disappeared. In other words the relative economic position of the creditor and the debtor country must have changed before a net reimbursement by the debtor country is justified. As has been correctly pointed out by Nurkse (5), this principle is generally accepted as far as internal public debt is concerned: a net repayment of such debt must be justified by the conditions of the economy and not on the basis of the terms of amortization of a particular loan. There is no reason why it should be otherwise in the field of foreign indebtedness.

In practice, however, we must recognize that the forms in which capital movements actually take place may give rise to difficulties. A capital exporting country is under no compulsion to refinance regularly the loans it has granted in the past by granting new ones; as, on the other hand, the amortization terms of the loans granted in the past are generally inflexible, an interruption or even a reversal of the flow capital may take place without being justified by any change in the basic economic conditions.

What seems important, though, is to keep separate the problem of amortization and the problem of interest payments. If we assume that a net outflow of capital must not take place until the economic position of the debtor country has changed in the sense indicated

(4) P. N. Rosenstein-Rodan, " Foreign Aid required for the Third Five-Year Plan in India ", M.I.T., Cambridge, Mass. 1959 (mimeographed).

(5) R. Nurkse, " Problems of Capital Formation in underdeveloped countries ", Oxford, 1953, p. 134.

above relative to that of the creditor countries, the amortization problem appears simply as a problem of liquidity, that is of ensuring the appropriate coincidence of capital inflows with outflows on amortization account. Any problem that may arise from a lack of coincidence of such flows, should be taken care of by recourse to complementary sources of international liquidity such as the International Monetary Fund.

The " burden " of the foreign debt and the determination of the level of sustainable indebtedness should therefore be studied only with reference to interest payments, at least in the context of the present hypothesis. (Of course the expression " interest payments " must be taken here in a broad sense, including both interest proper and other types of reward of the foreign capital invested in the country). Sustainable indebtedness has been defined as the indebtedness which results in a net outflow of interest payments that — considering the foreseeable development of the " goods and services " account of the balance of payments — can be covered without disturbing the equilibrium of the economy and without raising the cost of servicing foreign capital to levels unjustified by the yield of the investment which it has financed.

To give a concrete example, one may say that indebtedness will have overtaken the " sustainable " level when interest payments can be covered only at the cost of a reduction in essential imports. On the other hand, if such imports and the regular service of the foreign debt can be maintained only at the cost of gradual depreciation of the country's currency — so as to encourage exports and restrain imports — the consequent worsening of the terms of trade might raise the cost of the foreign capital invested in the country to an economically unjustifiable level: in fact, the transfer problem can be reduced to the problem of the real cost of foreign capital.

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To the extent to which it may be necessary (for lack of a reliable forecast of balance of payments developments) to look for specific criteria to judge the desirability of granting a given loan, the consideration of the balance of payments effects of the projected investment may be an acceptable criterion. It would be much less acceptable to arrive at a decision by looking to see whether the period

needed for the technical amortization of the investment being considered remains within the maximum length of the loan which can be granted. If the aim in view is that of avoiding an excessive burden on the balance of payments of the debtor country, one must make sure, for lack of a better criterion, that investment is self-liquidating in terms of foreign currency. For this, it is neither necessary nor sufficient that the investment may be amortized in national currency within the maximum length of the foreign credit. Actually even a relatively short-term credit may be an acceptable means of finance for an investment which can be amortized only over a long period, but which yields immediate results in terms of foreign currency earnings: what remains to be done is obviously to refinance the credit in local currency by non-inflationary methods.

Conversely, the investment may have a high yield in local currency and therefore be amortizable over a short period but have little or no effect on foreign exchange earnings. It would be logical for the lender to take this circumstance into account while, at the same time, avoiding the mistake of favouring unduly the ultimate beneficiary of the loan, who may find in fact no difficulties in servicing it in local currency out of the return on the investment itself. The United States' Agency for International Development has recognized the existence of situations of this type; it has therefore agreed, in loans to foreign private enterprises that, where the repayment of such loans would unduly burden the receiving country's balance of payments, the loan agreement will permit the borrower to repay the loan to his own government in local currency, while permitting the latter to service the foreign debt on much softer terms, that is the terms that would apply if the government had taken the loan directly from the A.I.D.

Let us now try to sum up the reasoning developed so far. In order to determine the level of sustainable indebtedness we must think of a situation where equilibrium has been established between the new gross inflow of foreign capital and the amortization of the outstanding debt: under such circumstances, the level of sustainable indebtedness is a function of the rate of return paid to foreign capital and of the margin which can be found in the " goods and services " account to cover such return. This margin will be very modest in the take-off stage but may gradually increase with the development of national product. The ceiling which we have agreed to call

" sustainable indebtedness " will therefore be raised gradually, but it is clear that what a rapidly developing country needs is to be able to absorb a massive dose of foreign capital in the take-off stage. It is therefore in line with economic orthodoxy that in the first stages of the process of development not only amortization on the outstanding debt but also interest payments be covered by the inflow of fresh foreign capital, until the moment when the level of indebtedness sustainable in the long run by the economy has been reached. From such point on — and as long as the relative scarcity of capital in the given country and in the creditor countries will remain substantially unchanged — a surplus in the other items of the current account will be needed to cover the payment of interest, the new inflow of capital covering " ex hypothesi " the annual amortization payments.

After having sketched the economic background of the problem we have now to take into account the different factors which in practice determine the possibility of applying the concepts described above. We shall have to examine:

(a) the interest conditions on which capital can be obtained;

(b) the terms of amortization of the credits obtained from abroad and, particularly, the duration, the initial grace period and the schedule of reimbursement;

(c) any special clauses, such as reimbursement in local currency, which modify the balance of payments burden of the service of a given foreign loan.

4. The burden of the remuneration of foreign capital

It is appropriate, in considering the concrete aspects of this problem, to introduce a distinction between interest payments on capital obtained from public or semi-public sources abroad and, on the other hand, interest and dividend payments on private foreign capital. The rate of return on private capital must be generally considered by the creditor as well as by the debtor country as an aspect of the problem on which neither can exert any control. As far as public and semi-public foreign capital is concerned, one may say instead that the rate of interest to be paid is, to a lesser or greater

extent, a " political price ", that is a price which is not set by the market. The fact that capital channelled to developing countries by foreign public sources has been obtained by recourse to the market is in itself irrelevant: the rate which will be paid on the market in such cases will be determined by the credit standing of the public body acting as intermediary and certainly not by the credit standing of the final beneficiary of the funds, that is the developing country.

It would actually be more accurate to say that an international capital market does not exist for developing countries in the same sense in which it exists for advanced countries or for large financial and industrial enterprises operating on an international basis. This can be explained by the poor rating as credit risks which market gives to new, capital-needy countries: only when risk is eliminated by an intervention of the State as a guarantor or as a channel of finance, is the market willing to provide the means needed for lending to developing countries. Therefore the market mechanism does not come into play for the allocation of capital among the countries in need of such an assistance: it is rather the governments of the capital-lending countries who have to arrive at a partly political, partly technical judgment on the allocation of the funds and on the terms on which such funds may be lent.

If the market is unable to give any indications on the interest rate which should be applied to the loans granted to developing countries, governments and international financial institutions need nevertheless some standard of judgment in their day-to-day operations, failing which they would be unable to follow a consistent policy line. However, the " doctrines " which have been developed in this field and the policies by which they have been implemented diverge considerably from country to country: this supports the contention that such " doctrines " are actually simple political options.

Perhaps the most wide-spread " doctrine " is that the rate applicable to loans to developing countries should be closely linked to the rate which the lending institution must pay when it borrows on the market. Such is for instance the policy followed by the International Bank for Reconstruction and Development, by the Export-Import Bank of Washington and by the British Government, as far as the so-called " section 3 loans " are concerned.

A more flexible policy is that of applying interest rates which are related to the nature of the investment which must be financed

abroad or to the financial situation of the capital-importing country, even if such rates must be kept below the market level. This policy can best be applied if the lender can rely on budgetary funds as well as on resources obtained on the capital market. The lending activities of Germany — through the Kreditanstalt für Wiederaufbau —, of France — with the Caisse Centrale de Coopération Economique —, and of the European Economic Community — in its recent Treaty of Association with Greece — appear to follow the doctrine that certain types of investment should be financed at concessionary rates, while others can bear the full market rate.

Finally, the policies implemented by the Agency for International Development in the United States and by the International Development Association abandon any reference to market rates. Both these institutions have actually adopted the principle of granting loans which are not only repayable on a very long period but are also practically exempt from interest payments; this policy is justified by referring to the impossibility of many less-developed countries shouldering any further balance of payments burden on account of the service of foreign indebtedness.

It is apparent that none of the three "doctrines" mentioned above is fully satisfactory and justifiable on rational bases. The first one would appear to imply that the lender simply takes into account the reality of the market which it is not within his power to modify. However, this point of view is hard to defend, for two reasons: in the first place because the lending institution is not faced with one single "market rate", but can play on the whole scale of interest rates existing on the market by choosing the most appropriate form of borrowing; in the second place, once it is accepted that the lending activities of such institution have no lucrative character, nothing prevents the government which controls the policy of such institution from providing out of budgetary funds the means necessary to cover the difference between the market rates and the concessionary rates granted to the developing countries. In fact, this method, like the recourse to State guarantees, will become increasingly important in the future, given the fact that it makes it possible to grant substantial assistance to developing countries at tolerable rates by tapping the private capital market.

When we turn to the doctrine which advocates linking the interest rate charged on foreign loans to the expected yield of the

investment which is to be financed by such loans, we meet again with a host of difficulties. Such difficulties concern the estimate of the expected yield, and also the possible discrepancy between such yield in local currency and the ability of the new investment to generate additional foreign currency earnings, which is the most directly relevant factor with respect to the service of the foreign debt (see above paragraph 3).

Finally there is the criterion which links the interest rate to the economic conditions and, more particularly, to the balance of payments situation of the capital-importing country. This criterion would appear to be the most appropriate when the "aid" aspect of loans granted to developing countries must be stressed, but a certain number of objections can be raised against it, the most frequent of which is that developing countries are thus discouraged from adopting a realistic balance of payments policy. It must also be added that the mentioned criterion can only be applied rather arbitrarily, both because of the difficulties which are found in estimating the likely developments in the foreign payments situation of the receiving countries and because of the need to avoid a discriminatory treatment from country to country. From the technical point of view one must also remember that the aim sought by granting particularly low-interest rates can also be pursued by introducing in loan contracts certain clauses, which give greater flexibility to interest payments, allowing the debtor to postpone such payments for one or more years in case of evident balance of payments difficulties.

In conclusion it is difficult to offer a rational basis for the choice of the interest rates which ought to be charged on financial assistance to developing countries. Such a choice is essentially political and, at the same time, will be strongly influenced by the ways in which lending countries organize their development assistance. One aspect, which should not be forgotten is that the financial assistance of public or semi-public institutions will have to play an equilibrating role, from the standpoint of the terms of lending, with respect to the other sources of finance to which developing countries may have access. Such terms will be decisive in determining whether developing countries can absorb enough foreign capital without, at the same time, acquiring debt servicing obligations too heavy for balance of payments equilibrium.

5. The terms of repayment for foreign loans

Having already discussed the importance of amortization charges in estimating a country's ability to borrow more abroad we can sum up once more in a few words. Though it is true that on a theoretical plane the terms of reimbursement are *not* a significant element in determining sustainable indebtedness, one must also recognize that in practice the problem of amortization may have to be given careful attention. In fact, if the expected renewal or refinancing of maturing loans do not occur, a net deficit on capital account may appear: the danger of such a development occurring in practice is, of course, particularly serious for capital-importing countries that rely for the financing of their investments on medium-term, rather than long-term, credits from abroad.

The data gathered by the World Bank in recent years (which are presented as an annex to this paper) show that the two most important modifications of foreign indebtedness in the post-war years consist of a very significant increase of the total volume of such indebtedness and a reduction of the average term of foreign loans. Thus, in the period from 1956 to 1958, medium and long-term indebtedness in the low-income countries in Asia, the Middle East and Africa has practically doubled, and has increased by 40% in Latin America; the years gone by since the end of 1958 have witnessed a further strengthening of this trend. As for the average term of such debts, the studies of the World Bank show that, while at the end of the war the term of the external public debt of Latin America could be estimated at about 28 years — in the hypothesis that no new debt obligations were entered into — at the end of the first post-war decade this period had decreased to 11 years. This phenomenon can be traced in a very evident fashion by looking at the change in the proportions respectively of amortization and of interest payments in the data which are available on the service of external debt by developing countries: the percentage of amortization payments on total debt service appears to have significantly increased in the majority of cases.

In the past the increase in indebtedness and reduction in the average amortization period just mentioned have often been considered as the result of irresponsible export promotion by an excessive extension of medium-term credits to developing countries. To-day

a more balanced view seems to prevail: it is recognized that the availability of long-term capital for the finance of investments in developing countries is objectively insufficient and therefore such countries are compelled to have recourse to foreign medium-term borrowing in order to fill the gap. Capital-exporting countries have understood by now the serious consequences which such a trend could have for the solvency of less-developed economies. They have therefore recognized the desirability of adapting the terms of public capital assistance so as to provide a balancing element in the structure of the foreign debt of low-income countries.

Thus there is a tendency to allow much longer amortization periods than those which are current in the commercial field and even longer than those which apply to the lenders' operations on their own capital markets. In the second place there has been a greater willingness to defer the beginning of amortization until several years after the disbursement of the loan. For instance, the International Development Association on one side, and the United States' Agency for International Development have been willing to grant loans whose total duration may attain fifty years and whose reimbursement will only start after a grace period of ten years. Another technique which has sometimes (6) been suggested is the following: for loans to low-income countries the amortization schedule should stipulate that reimbursement takes place by equal instalments of capital and interest, with a substantial grace period. However, if the service payments could not take place at the due dates for balance of payments reasons, the payment of the instalments could be postponed and interest at the current World Bank rate would be charged on them.

Whatever their merits in financial terms, it must be recognized that such extended repayment schedules with long grace periods appear very often justified in the light of the needs of developing countries: the massive infrastructure investments they must make in the "take-off" stage are likely to have at least for a number of years a low direct yield and can therefore contribute little to the amortization of the loans with which they are financed from abroad.

On the other hand, it is clear that a wide-spread adoption of such lending techniques, even if only for the assistance provided

(6) See for instance P. Hoffman, "100 countries, 1 ¼ billion people", Committee for International Economic Growth, New York, 1959, p. 52.

by governments and public institutions, would present a series of complex problems for the lenders. In the first place, many countries are reluctant, for political reasons, to provide such assistance on the basis of budgetary funds. It is a fact that governments often feel that assistance given indirectly through special lending institutions having recourse to the market rather than directly, out of tax receipts, can more easily be "sold" to public opinion and to Parliaments. If this is so, however, one stumbles into the practical impossibility of borrowing on the capital market for periods as extended as those of the loans granted to developing countries. The obstacle is less serious than it might seem, if one considers that public financial institutions are not bound to such a strict respect of "financial orthodoxy" as private financial institutions are. One must agree that it is perfectly compatible with sound financial management that such institutions enter into commitments towards their capital suppliers for shorter terms than those applying to repayment commitments they themselves obtain from the foreign borrowers. An appropriate management of the lending institutions' finances would make it possible to renew periodically, whenever necessary, their commitments towards the market, without waiting for the reimbursement of the foreign credits. As for the problem of the gap between market rates and the rates at which loans would be granted to the developing countries, there is no need to repeat the considerations presented already in the preceding paragraph.

6. Local currency repayment of foreign loans

We still have to examine the special clauses which permit the beneficiary of the loan to repay the lender in local currency or in locally produced goods. In general, one might say that such currency clauses — to the extent that the sums repaid are transferred abroad through the purchase of local currencies — amount to something very close to multiple-price or multiple-exchange rate practices characteristic of commercial bilateralism. If the goods purchased with the local currency credited to the lender were actually valued at the prices at which they normally enter international trade, it is hard to see what would be the use of the clause permitting repayment in local currency: it would be just as easy for the borrower to agree to repayment in foreign currency.

More frequently, however, the local currency funds credited to the lending country on interest and amortization account are not designed to be transferred but rather to be re-lent to the country which has just reimbursed them. As a consequence the repayment procedure takes the character of a pure accounting fiction and the economic substance of the transaction becomes that of a simple grant. The difference with respect to a grant consists in the control which the lending country keeps on the use of the local currency repaid by the borrower; thus a certain influence can be exercised on the new investments financed by such funds in the beneficiary country. Over and above such a control on the direction of investment — which is however often purely nominal — one could also say that the government of the beneficiary country has to submit to a certain discipline because of the fact that it must accumulate through the state budget or in any other way the resources needed to carry out the reimbursement in local currency.

So much for the asset side; on the liability side we must first put the political problems created by the accumulation in the hands of a foreign government of substantial local currency balances and the fact that this appears to give such government an undue influence in the life of the country. But even on the purely financial level, the recourse to local currency repayment presents some major difficulties. One need only be reminded that less-developed countries often meet such problems in balancing their budgets that the reimbursement is carried out simply by the creation of new money: when such a money is lent again by the creditor governments to the same country and spent for new investments, the effects are likely to be inflationary. Instead of being an incentive to financial orthodoxy, such loans repayable in local currency may then contribute to financial disorder in the borrowing country.

This is particularly striking when one considers the snowballing effects — by the operation of the mechanism of compound interest — of the increase of the local currency balances repaid to the lending country. Truly staggering results are obtaining if one examines the increase of such local currency balances. Let us take as original conditions of the loans an interest of 4% and a total duration of forty years: we can then see that, in the hypothesis

that the local currency reimbursed is immediately re-lent to the government of the developing country, at the end of the period stipulated for the reimbursement of the original loan (that is at the end of forty years) the total local currency indebtedness towards the lending country would amount to nearly seven times the original loan.

Summing up, it does not seem correct to consider loans bearing interest at market conditions but repayable in local currency to be an acceptable compromise between, on one side, loans at concessionary rates and with long amortization periods and, on the other, simple grants. Loans which can be reimbursed in local currency seem to possess the majority of the disadvantages of both forms without having their advantages. Suffice it to mention that they appear as politically delicate as grants and as burdensome — from the point of view of internal finance — as loans, without, however, stimulating a healthy financial policy in the debtor country or limiting the taxpayers' sacrifices in the creditor country.

7. Conclusions

The study of the problems relating to the foreign indebtedness of developing countries appears to be a necessary condition for planning a rational policy of financial support of these countries. Too often in the past repercussions on the foreign indebtedness of the borrowing country have been either ignored, thus preparing for the future balance of payments difficulties which could have been avoided, or have, at the other extreme, been given undue weight and taken as a justification for refusal to support the development of economically promising countries.

The data given in the annex to this paper show the importance of the contribution of foreign capital to the financing of investments and of imports in some developing countries and, on the other hand, the heavy commitments which burden some countries' receipts as a consequence of past recourse to foreign capital. Even more important, these data show how widely the situation differs from country to country. Such differences eloquently point out the danger of applying general criteria of judgment in this field and the necessity of examining, in mapping out assistance policy to a given country, the actual burden of indebtedness which the country can sustain in

the long run. If the interest burden deriving from a foreign assistance justified by the investment needs of the country were to appear excessive, then we have to draw the appropriate conclusions in determining the conditions on which such assistance may be given.

It is clear that the resources of capital-exporting countries are limited and that the needs of developing economies can only be satisfied partially and gradually. In fact, even the absorptive capacity of foreign capital by such countries is, as is well known, limited on technical grounds. What is needed is therefore that countries providing such assistance bilaterally or multilaterally, once they are satisfied that the programs to be financed are economically sound, should not be discouraged by the consequences which financing of such programs at normal interest and reimbursement conditions may have on the payments situation of the borrowing country. It will be necessary instead, in such circumstances, to look for the form of financial support which makes it possible to exploit fully the economic potentialities of the country without bringing it to the verge of a financial crisis. The range of financial instruments available for assistance to less-developed countries is sufficiently extended to ensure that such an objective can be reached. It will, however, be necessary to proceed to the examination of the situation of the main developing countries one by one and to draw up concerted plans of action within the organisations which are entrusted with the coordination of the development assistance activities.

Brussels CLAUDIO SEGRÉ

STATISTICAL ANNEX

Table I

PUBLIC DEBT SERVICE RATIO, RATIO OF SERVICE PAYMENTS ON PRIVATE ACCOUNT AND RATIO OF TOTAL SERVICE PAYMENTS TO EXTERNAL RECEIPTS

Countries	1955			1958		
	Public	Private	Total	Public	Private	Total
Asia, Middle East and Africa						
Ceylon	0.5	4.1	4.6	0.5	3.6	4.1
Indonesia	3.8	11.4	15.2	3.5	10.2	13.7
Iraq	0.0	37.0	37.0	0.0	36.0	36.0
Philippines	1.5	11.6	13.1	2.1	8.9	11.0
United Arab Republic	0.2	5.7	5.9	0.2	0.8	1.0
Burma	0.5	0.9	1.4	1.5	2.1	3.6
India	0.7	1.0	1.7	1.7	3.2	4.9
Iran	1.3	24.4	25.7	5.5	31.9	37.4
Pakistan	2.3	2.4	4.7	5.3	1.8	7.1
Thailand	1.1	1.9	3.0	2.3	3.2	5.5
Fed. of Rhodesia and Nyasaland	2.7	17.1	19.8	4.2	12.8	17.0
Belgian Congo	1.7	11.3	13.0	4.0	11.7	15.7
Ethiopia	0.4	2.3	2.7	1.9	4.8	6.7
Latin America						
Brazil	19.7	5.3	25.0	13.0	5.6	18.6
Bolivia	4.8	2.9	7.7	4.0	0.6	4.6
Costa Rica	0.9	7.9	8.8	4.2	7.2	11.4
Cuba	1.0	6.7	7.7	0.6	6.7	7.3
Nicaragua	4.9	8.8	13.7	4.7	4.0	8.7
Paraguay	4.3	1.7	6.0	4.2	1.5	5.7
Venezuela	n.a.	29.4	29.4	n.a.	24.6	24.6
Chile	8.8	13.0	21.8	13.2	11.9	25.1
Colombia	6.1	0.6	6.7	21.4	7.8	29.2
Ecuador	4.0	14.2	18.2	9.8	12.7	22.5
El Salvador	1.0	2.0	3.0	1.4	2.0	3.4
Guatemala	0.2	5.6	5.8	0.7	2.9	3.6
Haiti	6.5	2.2	8.7	9.3	0.0	9.3
Honduras	0.0	0.0	0.0	1.8	2.9	4.7
Mexico	7.7	6.0	13.7	9.0	8.9	17.9
Panama	0.7	13.9	14.6	4.9	10.5	15.4
Peru	4.9	6.1	11.0	7.6	7.7	15.3
Uruguay	5.6	1.5	7.1	7.1	0.8	7.9
Australia	5.0	8.6	13.6	6.3	10.0	16.3
Union of South Africa	2.0	9.6	11.6	3.2	11.8	15.0
Japan	5.4	1.4	6.8	5.3	1.2	6.5
European Capital Importers						
Austria	1.5	0.3	1.8	1.1	0.9	2.0
Finland	2.8	0.4	3.2	2.7	0.5	3.2
Iceland	2.0	0.5	2.5	3.6	0.7	4.3
Italy	2.0	1.0	3.0	2.0	1.6	3.6
Norway	2.1	1.2	3.3	2.9	2.0	4.9
Greece	2.9	1.0	3.9	1.7	0.5	2.2
Yugoslavia	13.2	1.0	14.2	6.8	0.8	7.6

Source: Dragoslav Avramovic and Ravi Gulhati, *op. cit.*

Table II

RATIO OF TOTAL CAPITAL IMPORTS TO EXPORT EARNINGS

(average 1956-1958, in %)

Country	%	Country	%
South Korea	1.567	Burma	20
Pakistan	489	Philippines	19
Jordan	463	Ethiopia	18
Viet-Nam	362	Paraguay	16
Lybia	239	Iran	16
Israel	169	Former British West Africa	16
Somaliland	77	Thailand	13
Formosa	76	Chile	12
Algeria	76	Dominican Republic	12
Former French African Territories	64	Indonesia	12
Fed. of Rhodesia and Nyasaland	46	Costa Rica	12
Bolivia	44	Nicaragua	11
Greece	43	Other Territories under British Trusteeship	10
Turkey	42	Ecuador	9
Antilles	39	Cuba	8
Peru	36	Iraq	8
Liberia	34	Colombia	6
Guatemala	34	Ghana	5
Panama	32	Sudan	5
India	32	United Arab Republic	5
Yugoslavia	31	Argentina	4
Mexico	24	Uruguay	4
Surinam	23	Honduras	3
British East Africa	22	Lebanon	3
Brazil	21	Malaya and Singapore	2
Spain	20	Ceylon	1
Venezuela	20	El Salvador	1
Congo (Leopoldville)	20		

Source: Dragoslav Avramovic and Ravi Gulhati, *op. cit.*
O.E.E.C., " Moyens financiers mis à la disposition des pays en voie de développement économique, 1956-59 ", Paris, 1961.
I.M.F., " Balance of Payments Yearbooks ".

TABLE III

RATIOS OF CAPITAL FORMATION, CAPITAL IMPORTS AND DOMESTIC SAVINGS TO G.N.P.

(average 1956-1958, in %)

	Ratio of capital formation to G.N.P.	Ratio of capital imports to G.N.P.	Ratio of domestic savings to G.N.P.	Ratio of capital imports to capital formation
Fed. of Rhodesia and Nyasaland	35	17.9	17	51
Israel	27	13.1	14	49
Peru	27	6.7	20	25
Venezuela	26	8.6	17	33
Congo (Leopoldville)	26	9.0	16	35
Iraq	26	3.7	22	14
Antilles	24	12.4	12	52
Yugoslavia	22	1.6	21	7
Argentina	21	0.3	21	1
Algeria	21	13.6	8	65
Burma	20	4.1	16	21
Cuba	19	2.4	16	13
Dominican Republic	18	2.8	16	16
Costa Rica	18	2.7	16	15
Spain	18	0.9	17	5
Greece	16	3.5	13	22
Former French African Territories	15	10.6	5	71
Guatemala	15	6.1	9	41
Mexico	15	2.2	13	15
Panama	15	6.5	8	43
Former British West Africa	14	3.0	11	21
Former British East Africa	14	6.3	8	45
India	14	1.6	12	11
Lebanon	14	4.1	10	29
Formosa	14	9.0	5	64
Ecuador	13	1.6	12	12
Turkey	13	1.6	12	12
Thailand	13	2.3	10	18
Ghana	12	1.2	11	10
Brazil	12	1.7	11	14
South Korea	12	10.8	1	90
Ceylon	12	0.4	11	3
Colombia	12	0.9	11	8
Chile	10	1.7	8	17
Egypt (U.A.R.)	9	0.6	9	7
Philippines	8	1.7	7	21
Sudan	7	0.8	6	11

Source: DRAGOSLAV AVRAMOVIC and RAVI GULHATI, *op. cit.*

O.E.E.C., " Moyens financiers mis à la disposition des pays en voie de développement économique, 1956-59 ", Paris, 1961.

I.M.F., " Balance of Payments Yearbooks ".